(4)

No. 95-1086

Supreme Court, U.S.
FILED
MAR 1 1996
CLERK

IN THE

# Supreme Court of the United States

OCTOBER TERM, 1995

EMILY DISTAJO, et al.,

*Petitioners,*

vs.

DOCTOR'S ASSOCIATES, INC.,

*Respondent.*

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

## APPENDIX TO BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

MARK R. KRAVITZ*
KEVIN M. KENNEDY
WIGGIN & DANA
*Attorneys for Respondent*
One Century Tower
P.O. Box 1832
New Haven, Connecticut 06508-1832
(203) 498-4400

* *Counsel of Record*

98 pp

# APPENDIX TO BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

## TABLE OF CONTENTS


| | | Page |
|---|---|---|
| A. | September 12, 1995 Opinion of the United States Court of Appeals for the Second Circuit, filed in *Doctor's Associates, Inc. v. Emily Distajo, et al.*, U.S.C.A. Nos. 1724, 1725, 1726, 1988 ..... | A-1 |
| B. | September 28, 1995 Order amending the September 12, 1995 Opinion of the United States Court of Appeals for the Second Circuit, filed in *Doctor's Associates, Inc. v. Emily Distajo, et al.*, U.S.C.A. Nos. 1724, 1725, 1726, 1988 ..... | A-39 |
| C. | September 29, 1994 Order of the United States District Court for the District of Connecticut, filed in *Doctor's Associates, Inc. v. Emily Distajo, et al.*, U.S.D.C. No. 3:94cv00349 ..... | A-41 |
| D. | December 9, 1994 Ruling of the United States District Court for the District of Connecticut on Pending Motions, filed in *Doctor's Associates, Inc. v. Emily Distajo, et al.*, U.S.D.C. No. 3:94cv00349 ..... | A-50 |
| E. | May 3, 1994 Order and May 18, 1994 Amended Order of the General Superior Court of Justice, Gaston County, North Carolina, filed in *Michael Johnson v. Doctor's Associates, Inc., et al.*, 93 CvS 1324..... | A-54 |
| F. | May 18, 1994 Order of the General Superior Court of Justice, Gaston County, North Carolina, filed in *Michael Johnson v. Doctor's Associates, Inc., et al.*, 93 CvS 1324..... | A-59 |

| | | Page |
|---|---|---|
| G. | November 14, 1995 Order of the United States Court of Appeals for the Second Circuit, filed in *Doctor's Associates, Inc. v Distajo, et al.*, U.S.C.A. Nos. 1724, 1725, 1726, 1988 ..... | A-61 |
| H. | The Federal Arbitration Act, 9 U.S.C. §§ 1-4... | A-63 |
| I. | October 2, 1995 Motion to the Supreme Court of Illinois for a Supervisory Order Pursuant to Illinois Supreme Court Rule 383, filed in *Emily Distajo, et al. v. Doctor's Associates, Inc., et al.*, Supreme Court of Illinois Case No. 79878 ..... | A-66 |
| J. | October 31, 1995 Order of the Supreme Court of Illinois in *Emily Distajo, et al. v. Doctor's Associates, Inc., et al.*, Supreme Court of Illinois Case No. 79878 ..... | A-93 |
| K. | August 5, 1994 Affidavit of David G. Loseman, filed in the United States District Court for the District of Connecticut in *Doctor's Associates, Inc. v. Emily Distajo, et al.*, U.S.D.C. No. 3:94cv00349..... | A-94 |

**APPENDIX A**

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 1724, 1725, 1726, 1988 August Term, 1994

(Argued: June 7, 1995 Decided: Sep 12, 1995)

Docket Nos. 94-9207, 94-9293, 94-9209, 95-7183

DOCTOR'S ASSOCIATES, INC.,

*Plaintiff-Appellee,*

v.

EMILY DISTAJO, RENATO DISTAJO, CONSTANTINO LAMANDO, MILO LAMANDO, JOSE ALBERTO BRENES, ALVARO GUERRERO, MARIA T. GUERRERO, WESAM S. YOUMARAN, LINDA YOUMARAN, JULIE SHINO, JOHNSON SHINO, ALBERT YONAN, LEYLAH YONAN, LOUIS LOENNEKE, MARY ANN BOOKOUT, MICHAEL JOHNSON, DEBORAH A. KANE, GREGORY F. KANE, BRUNO GIANINNI, RONALD ROTHMUND, PATRICIA ROTHMUND, JOHN S. PAPALEO, JOHN A. McCRARY, JOHN GILLON, SONYA SMITH, PAUL RIISE, MELISSA RIISE, and RHONDA BENTON,

*Defendants-Appellants.*

and

DOCTOR'S ASSOCIATES, INC.,

*Plaintiff-Appellee,*

v.

RAYMOND BICKEL and SANDRA BICKEL,

*Defendants-Appellants.*

Before: MINER, LEVAL and CABRANES, *Circuit Judges.*

Appeal from several orders of the United States District Court for the District of Connecticut (Peter C. Dorsey, *Chief Judge*), denying certain appellants' motions to dismiss, granting appellee's petitions to compel arbitration, and entering a preliminary injunction barring appellants from pursuing parallel state litigation. Appellants contend that (1) the district court lacked subject matter jurisdiction; (2) the district court should have accorded preclusive effect to judgments entered in state courts against DAI; (3) the arbitration clause is void for "lack of mutuality"; (4) DAI waived its right to compel arbitration by initiating litigation through a shell corporation; and (5) the district court should have decided whether the appellants were fraudulently induced to enter the arbitration agreement, rather than leaving that question for the arbitrators.

Reversed in part and affirmed in part.

DAVID M. DUREE, Reinert, Duree & Crane, St. Louis, Missouri, *for Defendants-Appellants Emily Distajo, Renato Distajo, Constantino Lamando, Milo Lamando, Jose Brenes, Alvaro Guerrero, Maria Guerrero, Wesam Youmaran, Linda Youmaran, Julie Shino, Johnson Shino, Albert Yonan, Leylah Yonan, Louis Loenneke, Mary Ann Bookout, Michael Johnson, Deborah A. Kane, Gregory F. Kane, Bruno Gianinni, Ronald Rothmund, Patricia Rothmund, John S. Papaleo, Raymond Bickel and Sandra Bickel.*

Edward E. Angwin, Birmingham, Alabama, *for Defendants-Appellants John A. McCrary, John Gillon, Sonya Smith, Paul Riise, Melissa Riise, and Rhonda Benton.*

Nicholas Wocl, Tooher, Puzzuoli & Wocl, Stamford, Connecticut, *for all Defendants-Appellants.*

Edward Wood Dunham, Wiggin & Dana, New Haven, Connecticut, *for Plaintiff-Appellee.*

JOSÉ A. CABRANES, *Circuit Judge:*

This case is about forum-shopping, by one and all. Doctor's Associates, Inc. ("DAI") is the national franchisor of Subway sandwich shops. DAI and its franchisees entered into standard franchise agreements, which required them to arbitrate all contractual disputes in Bridgeport, Connecticut, under Connecticut law. When problems did arise, however, neither side invoked the arbitration clause. First, DAI directed its wholly owned real-estate leasing companies to bring summary eviction proceedings against the franchisees in local state courts.[1] The franchisees, in turn, scrambled to obtain judgments against DAI in local state courts.

When DAI found itself faced with state court claims around the country, it sought shelter in the arbitration clause of its franchise agreements. Accordingly, it petitioned the federal district court in Connecticut to compel arbitration under the Federal Arbitration Act. Before the district court could act, some of the franchisees won state court judgments against DAI. But DAI eventually convinced the district court to enjoin the franchisees from pursuing their state actions--even from enforcing judgments already entered--and to send the parties to Bridgeport to resolve their disputes around the arbitral table.

On appeal, we are presented with several questions relating to the Federal Arbitration Act: (1) whether a district court has

---

[1] DAI and other franchisees have been involved in similar litigation around the country. *See, e.g., Kroll v. Doctor's Assocs., Inc.*, 3 F.3d 1167 (7th Cir. 1993); *Mosca v. Doctors Assocs., Inc.*, 852 F. Supp. 152 (E.D.N.Y. 1993); *Wilson v. Subway Sandwiches Shops, Inc.*, 823 F. Supp. 194 (S.D.N.Y. 1993); *In re Sims*, 1991 U.S. Dist. LEXIS 13664 (E.D. La. 1991); *Yates v. Doctor's Assocs., Inc.*, 193 Ill. App. 3d 431, 549 N.E.2d 1010 (5th Dist. 1990); *Cox v. Doctor's Assocs., Inc.*, 245 Ill. App. 3d 186, 613 N.E.2d 1306 (5th Dist.), *appeal denied*, 152 Ill.2d 556 (1993), *cert. denied*, 114 S. Ct. 1069 (1994); *Casarotto v. Lombardi*, 268 Mont. 369, 886 P.2d 931 (1994), *vacated and remanded*, 115 S. Ct. 2552 (1995).

The relationship between DAI and the Bickels' landlord has also been the subject of litigation. *Jannotta v. Subway Sandwich Shops, Inc.*, 1995 U.S. Dist. LEXIS 7586 (N.D. Ill. 1995).

subject matter jurisdiction over a petition to compel arbitration where there is complete diversity among all the parties to the arbitration agreement (all of whom are joined as parties in the petition), but where other, nondiverse parties have been joined as defendants in a parallel state action involving the same underlying dispute; (2) whether the district court should have accorded preclusive effect to various state court judgments entered in Alabama, Illinois, and North Carolina courts; (3) whether an arbitration clause is void for "lack of mutuality" under Connecticut law if it requires only one party to submit disputes to arbitration; (4) whether a party to an arbitration agreement waives its right to compel arbitration when it litigates substantial issues through an alter ego; and (5) whether a district court or an arbitrator should decide whether a party was fraudulently induced to assent to an arbitration agreement.

The district court found complete diversity, refused to accord preclusive effect to the state court judgments, found that the arbitration clause did not lack mutuality, held that DAI had not waived its right to arbitrate regardless of whether its leasing affiliates, which brought the court proceedings, were its alter egos, and left the question of fraudulent inducement to the arbitrators. As discussed below, we affirm in part and reverse in part.

## I. FACTS

Doctor's Associates, Inc. ("DAI"), a Florida corporation, is the national franchisor of "Subway" sandwich shops. DAI entered into identical franchise agreements with each of the defendant franchisees (the "Franchisees").[2] Each agreement

---

[2] For convenience, we shall refer to the franchisees individually according to the following case numbers, or collectively according to the state in which they brought suit, e.g., the "Alabama franchisees." We list the district court docket number, as well as the state of each group of franchisees whose cases were consolidated under the heading of *Doctor's Associates, Inc. v. Distajo*:

Case #1: 3:94-CV-349 *Doctor's Associates, Inc. v. Distajo* (IL)

*(Footnote continued)*

contains an identical arbitration clause, which provides that any claim arising out of or relating to the franchise agreement must be arbitrated in Bridgeport, Connecticut, under the Commercial Arbitration Rules of the American Arbitration Association. According to the arbitration clause, no party may take legal action against the other in connection with the franchise agreement without first attempting to arbitrate the dispute.[3]

---

| | |
|---|---|
| Case #2: 3:94-CV-511 | *Doctor's Associates, Inc. v. Brenes* (IL) |
| Case #3: 3:94-CV-514 | *Doctor's Associates, Inc. v. Guerrero* (IL) |
| Case #4: 3:94-CV-515 | *Doctor's Associates, Inc. v. Youmaran* (IL) |
| Case #5: 3:94-CV-516 | *Doctor's Associates, Inc. v. Shino* (IL) |
| Case #6: 3:94-CV-517 | *Doctor's Associates, Inc. v. Loenneke* (IL) |
| Case #7: 3:94-CV-803 | *Doctor's Associates, Inc. v. Johnson* (NC) |
| Case #8: 3:94-CV-354 | *Doctor's Associates, Inc. v. McCrary* (AL) |
| Case #9: 3:94-CV-369 | *Doctor's Associates, Inc. v. Gillon* (AL) |
| Case #10: 3:94-CV-370 | *Doctor's Associates, Inc. v. Smith* (AL) |
| Case #11: 3:94-CV-371 | *Doctor's Associates, Inc. v. Risse* (AL) |
| Case #12: 3:94-CV-372 | *Doctor's Associates, Inc. v. Benton* (AL) |
| Case #13: 3:94-CV-948 | *Doctor's Associates, Inc. v. Kane* (MA) |
| Case #14: 3:94-CV-1108 | *Doctor's Associates, Inc. v. Giannini* (PA) |
| Case #15: 3:94-CV-1456 | *Doctor's Associates, Inc. v. Rothmund* (IL) |
| Case #16: 3:94-CV-1457 | *Doctor's Associates, Inc. v. Papaleo* (IL) |

Although *DAI v. Bickel* was not consolidated with the other sixteen cases before the district court, it was consolidated for purposes of oral argument before this court.

[3] The arbitration clause provides as follows:

> Any controversy or claim arising out of or relating to this contract or the breach thereof shall be settled by Arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association at a hearing to be held in

*(Footnote continued)*

DAI requires each franchisee to sublease its premises from one of several real-estate leasing companies that are wholly owned by DAI. Each sublease contains a "cross-default" provision, whereby any breach of the franchise agreement by the franchisee constitutes a breach of the sublease.[4] According to the deposition testimony of one of its own officers, DAI wanted its leasing affiliate to be the franchisees' sublessor to obtain greater leverage over them in the event of a dispute.

### A. *The District Court Proceedings in Doctor's Associates, Inc. v. Distajo (Nos. 94-9207, 94-9209, 94-9293)*

From 1991 through 1993, various disputes arose between DAI and the several franchisees. DAI never filed any demands for arbitration, despite its claims that the franchisees had breached the franchise agreements. Instead, DAI directed its leasing companies to invoke the cross-default provisions of the subleases, and to institute eviction proceedings in state courts against each franchisee.

In response to these eviction proceedings, each of the franchisees filed a state court action claiming, *inter alia*, fraud and breach of contract by DAI, its leasing companies, and several of DAI's officers and agents.

---

> Bridgeport, Connecticut and judgment upon an award rendered by the Arbitrator(s) may be entered in any court having jurisdiction thereof. The commencement of arbitration proceedings by an aggrieved party to settle disputes arising out of or relating to this contract is a condition precedent to the commencement of legal action by either party. The cost of such a proceeding will be borne equally by the parties.

[4] The cross-default provision reads in relevant part as follows:

> If at any time during the term of this Sublease, Sublessee shall default in the performance of any of the terms, covenants or conditions of the aforesaid Franchise Agreement . . . Sublessor, at its option, may terminate this lease . . . and upon such termination, Sublessee shall quit and surrender the leased premises to Sublessor . . . .

According to the franchisees, DAI uses this subleasing arrangement to circumvent the arbitration clause in the franchise agreements. They argue that the leasing companies are mere shells, or alter egos, of DAI. It is undisputed that the leasing companies are wholly owned by DAI, that they have no assets or net income, and that DAI decides when the leasing companies will file eviction proceedings. Pursuant to the sublease, the franchisee must pay rent directly to the actual landlord; no rent is paid to the leasing company. According to the franchisees, DAI has taken the position that the arbitration clause in the franchise agreement is not binding on its leasing companies, because they are not parties to that agreement. The franchisees claim also that the leasing companies have asserted the right to proceed with eviction lawsuits against the franchisees even if the franchisees file arbitration demands against DAI. Thus, DAI allegedly brought eviction lawsuits through its leasing companies to pressure its franchisees into resolving disputes, but invokes the arbitration clause to protect itself against litigation initiated by the franchisees.

DAI responded to each state lawsuit brought by the franchisees by serving a demand for arbitration pursuant to the franchise agreement. When the franchisees refused to arbitrate their disputes, DAI filed petitions to compel arbitration, pursuant to the Federal Arbitration Act, 9 U.S.C. § 4, in the United States District Court for the District of Connecticut. All sixteen cases were eventually consolidated before Chief Judge Peter C. Dorsey. Before the district court ruled on DAI's petitions, the state courts in Alabama, Illinois, and North Carolina entered judgments in favor of the franchisees in Cases 1-12 and 15-16.

In the district court, DAI contended that the franchisees were bound by the franchise agreement to submit any disputes with DAI to arbitration in Bridgeport, Connecticut, before instituting judicial proceedings. The franchisees responded by seeking dismissal of DAI's petitions on several grounds, including, *inter alia*: (1) lack of subject matter jurisdiction, due to incomplete diversity of the parties; and (2) collateral estoppel, based on the intervening state court judgments. The

district court rejected each of these contentions in a ruling dated September 29, 1994. The district court simultaneously rejected DAI's motion to enjoin the franchisees from pursuing parallel state court proceedings, on the grounds that the requested injunction did not fall within any of the narrow exceptions to the Anti-Injunction Act, 28 U.S.C. § 2283.

On November 10, 1994, the district court granted DAI's petitions to compel arbitration. In doing so, the court rejected several defenses raised by the franchisees, including the following: (1) that the arbitration clause was void for lack of mutuality; (2) that DAI had waived arbitration by virtue of its leasing companies' prosecution of eviction lawsuits; and (3) that DAI had fraudulently misrepresented the scope of the arbitration clause in the franchise agreement. The court held that the arbitrators, not the court, should determine whether the leasing companies were "alter egos" of DAI, and then address the question whether DAI had fraudulently misrepresented the scope of the arbitration agreement.

When the franchisees continued to pursue their state court actions, DAI obtained a temporary restraining order from the district court on November 22, 1994, preventing them from participating in the parallel state proceedings. On December 14, 1994, the district court entered a preliminary injunction, barring the Distajo franchisees from seeking enforcement of their Illinois judgment. *Doctor's Assocs., Inc. v. Distajo*, 870 F. Supp. 34 (D. Conn. 1994). The court concluded that injunctive relief was "not inappropriate" under the Anti-Injunction Act, 28 U.S.C. § 2283, because continued state litigation would "impair the integrity of the order of arbitration." In granting DAI's motion, the court rejected the franchisees' argument that an intervening judgment entered in favor of the Distajo franchisees by an Illinois state court on October 24, 1994, was "final" for *res judicata* purposes and would preclude entry of the injunction under the full faith and credit statute, 28 U.S.C. § 1738.

All of the franchisees filed timely appeals from the district court's order of September 29, 1994, denying their motions to

dismiss, and the order of November 10, 1994, compelling arbitration. All of the franchisees except those from Alabama (Cases 8-12) also appeal from the court's December 9, 1994, order entering the preliminary injunction.

### B. *The District Court Proceedings in Doctor's Associates, Inc. v. Bickel (No. 95-7183)*

The proceedings in the *Bickel* case differ somewhat from those cases consolidated under the *Distajo* rubric. On December 16, 1994, the Bickels filed a complaint in Illinois state court against DAI, its leasing company, its development agent, and three DAI officers. DAI responded by filing a petition to compel arbitration in the United States District Court for the District of Connecticut on January 20, 1995, and moved to enjoin the Bickels from prosecuting their state court action. On February 7, 1995, the Illinois court entered a default judgment against DAI. On February 13, 1995, Chief Judge Dorsey granted both DAI's petition to compel arbitration and its motion for a preliminary injunction, while permitting DAI to move the Illinois court to vacate the default judgment on the basis of defective service of process. The district court entered a written order embodying the *Bickel* injunction on May 9, 1995, but did not order DAI to post a bond.

The Bickels appeal from the court's order of May 9, 1995, granting DAI's petition to compel arbitration and entering the preliminary injunction.

## I. DISCUSSION

"When reviewing a district court's determination of its subject matter jurisdiction, we review factual findings for clear error and legal conclusions de novo." *In re Vogel Van & Storage, Inc.*, 59 F.3d 9, 11 (2d Cir. 1995). We also review *de novo* the district court's decision to compel arbitration. *Collins & Aikman Prods. Co. v. Building Systems, Inc.*, 58 F.3d 16, 19 (2d Cir. 1995).

**A. *Subject Matter Jurisdiction***

Section 4 of the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 1-16, confers jurisdiction on district courts to hear petitions to enforce arbitration agreements, but only to the extent that the court would otherwise have jurisdiction over the dispute. The statute provides as follows:

> A party aggrieved by the alleged . . . refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action . . . of the subject matter of *a suit arising out of the controversy between the parties*, for an order directing that such arbitration proceed in the manner provided for in such agreement.

9 U.S.C. § 4 (emphasis added). As the Supreme Court has explained,

> [t]he Arbitration Act is something of an anomaly in the field of federal-court jurisdiction. It creates a body of federal substantive law establishing and regulating the duty to honor an agreement to arbitrate, yet it does not create any independent federal-question jurisdiction under 28 U.S.C. § 1331 (1976 ed., Supp. V) or otherwise. Section 4 provides for an order compelling arbitration only when the federal district court would have jurisdiction over a suit on the underlying dispute; hence, there must be diversity of citizenship or some other independent basis for federal jurisdiction before the order can issue.

*Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 25 n.32 (1983).

The parties seem to agree that the only possible basis for federal subject matter jurisdiction in this case would be diversity of citizenship. 28 U.S.C. § 1332. It is a long-settled rule that in order to invoke diversity jurisdiction, the petitioner must show "complete diversity"--that is, that it does not

share citizenship with any defendant. *C.T. Carden v. Arkoma Assocs.*, 494 U.S. 185, 187 (1990); *Strawbridge v. Curtiss*, 7 U.S. (3 Cranch) 267, 267 (1806), *overruled on other grounds*, 43 U.S. (2 How.) 497, 555 (1844); *Curley v. Brignoli, Curley & Roberts Assocs.*, 915 F.2d 81, 84 (2d Cir. 1990), *cert. denied*, 499 U.S. 955 (1991). DAI is a Florida corporation with its principal place of business in Florida. The franchisees are residents of Alabama, Illinois, Massachusetts, North Carolina, and Pennsylvania.

The franchisees argue that there is not complete diversity of citizenship here. According to the franchisees, the "controvers[ies] between the parties" to which the FAA refers involve not only DAI, but also DAI's development agents--some of whom share the same citizenship with certain franchisees. None of those agents was a party to the franchise agreement; none has been joined as a party in the present proceeding. These local DAI agents, the franchisees contend, are "indispensable parties" to the present federal action, as evidenced by the fact that the affiliates are named defendants in the franchisees' state actions. In other words, the franchisees argue that their state court actions are the "suit[s] arising out of the controversy between the parties" hypothesized by the FAA. If so, then the citizenship of all the parties in the state actions determines whether there is complete diversity in the federal action to compel arbitration. Because these agents cannot be joined without destroying diversity, the franchisees argue that the district court should have dismissed the petitions to compel.

DAI responds that the "suit arising out of the controversy between the parties" is DAI's action to compel arbitration--not the parallel state action--and that DAI's affiliates are not "indispensable parties" to the federal action. Accordingly, DAI argues that we should look at the citizenship only of the parties named in the petition to compel, when determining whether there is diversity jurisdiction. *Prudential-Bache Sec., Inc. v. Fitch*, 966 F.2d 981, 988 (5th Cir. 1992) ("jurisdiction for a petition to compel arbitration [must] be determined from the face of the petition"). DAI offers a textual argument and a

policy argument to support its position. First, it notes that the FAA asks whether the district court would have jurisdiction over a suit arising out of a controversy "between the parties." The phrase "the parties" most sensibly refers to those persons who are parties to the arbitration agreement--and who therefore can be named in the petition to compel arbitration. Second, DAI argues that the FAA would be fatally undermined if "the parties" described in § 4 could be expanded to include persons who had not signed the arbitration clause but who allegedly were involved in the "underlying controversy." If such a rule were adopted, a party resisting arbitration could defeat federal jurisdiction simply by suing someone from the same state, plus the party seeking to compel arbitration, in a separate state lawsuit. Diversity would be destroyed simply by claiming that the local defendants in the parallel action were "indispensable parties" to the petition to compel.

We agree with DAI. The "parties" to which § 4 of the FAA refers are the parties to the petition to compel. As with any federal action, diversity of citizenship is determined by reference to the parties named in the proceeding before the district court, as well as any indispensable parties who must be joined pursuant to Rule 19 of the Federal Rules of Civil Procedure. Where joinder of a party would destroy subject matter jurisdiction, the court must dismiss the action if that party is "indispensable" to the litigation. Fed. R. Civ. P. 19(b),[5]

---

[5] Rule 19(b) provides:

Determination by Court Whenever Joinder not Feasible. If a person as described in subdivision (a)(1)-(2) hereof cannot be made a party, the court shall determine whether in equity and good conscience the action should proceed among the parties before it, or should be dismissed, the absent person being thus regarded as indispensable. The factors to be considered by the court include: first, to what extent a judgment rendered in the person's absence might be prejudicial to the person or those already parties; second, the extent to which, by protective provisions in the judgment, by the shaping of relief, or other measures, the prejudice can be lessened or avoided; third, whether a judgment rendered in the person's absence will be adequate; fourth, whether the plaintiff will have an adequate remedy if the action is dismissed for nonjoinder.

*Fluent v. Salamanca Indian Lease Auth.*, 928 F.2d 542, 548 (2d Cir.) (finding dismissal proper where indispensable party was Indian tribe that enjoyed sovereign immunity from suit), *cert. denied*, 502 U.S. 818 (1991). But individuals who are not parties to the arbitration agreement cannot be "indispensable" parties under Rule 19(b) if they do not meet either of the threshold tests of Rule 19(a).[6] That provision only requires joinder of a party if (1) the court cannot afford "complete relief" to those already joined, in the absence of that party, and (2) the unjoined party has an interest in the litigation and his absence may either impede his ability to protect that interest or subject the already-joined parties to a risk of inconsistent obligations--which often means the risk of piecemeal litigation. Neither condition is satisfied in the present case. First, the district court can grant all the relief sought by DAI in this case--an order compelling arbitration--regardless of whether DAI's development agents (nonparties to the arbitration agreement) are present. Second, the other consideration set forth in Rule 19(a)--possible prejudice resulting from piecemeal litigation--is overcome in this context by the FAA's strong bias in favor of arbitration. Indeed, the Supreme Court has categorically stated that the FAA requires courts to enforce an arbitration agreement "notwithstanding the presence of other persons who are parties to the underlying dispute but not to the arbitration agreement." *Moses H. Cone*, 460 U.S. at 20. A district court should not consider the citizenship of strangers to the arbitration contract, since they

---

[6] Rule 19(a) provides that

> A person who is subject to service of process and whose joinder will not deprive the court of jurisdiction over the subject matter of the action shall be joined as a party in the action if (1) in the person's absence complete relief cannot be accorded among those already parties, or (2) the person claims an interest relating to the subject of the action and is so situated that the disposition of the action in the person's absence may (i) as a practical matter impair or impede the person's ability to protect that interest or (ii) leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of the claimed interest.

are not "parties" the suit arising out of the controversy within the meaning of the FAA.

Accordingly, we hold that the district court was correct in looking only to the citizenship of the parties in the action before it--that is, DAI and the franchisees, who signed the arbitration agreement--to determine whether there was complete diversity. (JA 643) Because the parties conceded at oral argument that DAI and the franchisees are completely diverse, we affirm the district court's finding that it possessed subject matter jurisdiction pursuant to 28 U.S.C. § 1332 and 9 U.S.C. § 4.

**B. *Preclusive Effect of State Court Judgments***

The franchisees claim that the district court should have accorded full faith and credit to the various state court judgments that found the arbitration clause unenforceable in cases involving DAI and various of the defendant franchisees.

The full faith and credit statute, 28 U.S.C. § 1738, provides that "[state] judicial proceedings . . . shall have the same full faith and credit in every court within the United States . . . as they have by law or usage in the courts of such State . . . from which they are taken." Accordingly, a federal court must "give preclusive effect to state-court judgments whenever the courts of the State from which the judgments emerged would do so." *Allen v. McCurry*, 449 U.S. 90, 96 (1980); *Valley Disposal, Inc. v. Central Vermont Solid Waste Management Dist.*, 31 F.3d 89, 98 (2d Cir. 1994).

The parties agree that the question, therefore, is whether the various state court judgments (one in Alabama, eight in Illinois, and one in North Carolina) would be accorded preclusive effect under Alabama, Illinois, or North Carolina law, respectively. We address each state's law in turn.

**1. *The Alabama Judgment (Case # 8)***

During October 1993, DAI's real-estate leasing company and its equipment leasing company filed suit against franchisee John McCrary in the Circuit Court of Talladega County,

Alabama. In December 1993, McCrary filed a counterclaim against those DAI affiliates, and added DAI and its Alabama development agents as cross-claim defendants. On January 25, 1994, DAI and its affiliates filed a motion to dismiss the counterclaims and cross-claims or, in the alternative, to stay the Alabama case pending arbitration. DAI claims that it withdrew that motion after filing its petition to compel arbitration in the district court in Connecticut on March 8, 1994. On June 28, 1994, McCrary filed in the Alabama court a "Motion to Determine Non-Arbitrability of Issues."

On July 7, 1994, the Alabama Circuit Court ruled that the arbitration clause was void and unenforceable "for any of the following independent reasons": (1) lack of mutuality; (2) fraudulent inducement; (3) waiver by DAI of the right to invoke the arbitration clause; and (4) invalidity of the clause under Alabama law prohibiting all arbitration agreements, since the agreement lacked a sufficient "interstate nexus" to permit application of the FAA (which preempts state laws invalidating arbitration clauses affecting interstate commerce). The court also held that the issues raised in McCrary's counterclaim fell outside the scope of the arbitration clause. The Alabama court then expressly found "no just reason for delay" and accordingly directed that final judgment be entered in favor of McCrary.

DAI subsequently filed a motion for reconsideration, which the Alabama court denied on September 28, 1994. McCrary represents to this court that DAI subsequently appealed these orders to the Alabama Supreme Court. (The parties have been barred from proceeding with that appeal pursuant to the preliminary injunction entered by the district court on December 9, 1994.)

In an order entered September 29, 1994, denying McCrary's motion to dismiss, the district court declined to give preclusive effect to this Alabama judgment. The court reasoned that because a motion to reconsider the judgment was still pending in state court, there was not yet a final

judgment on the merits. Thus, principles of *res judicata* and collateral estoppel would not apply.

On appeal, DAI concedes that the Alabama ruling was indeed "final" for the purposes of preclusion. Under Alabama law, an order entered upon less than all of the claims presented in an action is a final, appealable order if "the judge makes an express determination that there is no just reason for delay . . . ." *Goza v. Everett*, 365 So. 2d 658, 659 (Ala. 1978). "Alabama courts, like federal courts, generally apply the same test of finality for purposes of preclusion as they do for appealability." *Stone v. Williams*, 970 F.2d 1043, 1055 (2d Cir. 1992), *cert. denied*, 113 S. Ct. 2331 (1993); *see also First Ala. Bank of Montgomery, N.A. v. Parsons Steel, Inc.*, 825 F.2d 1475, 1480 (11th Cir. 1987) (interpreting Alabama law), *cert. denied sub nom. McGregor v. First Ala. Bank of Montgomery*, 484 U.S. 1060 (1988). Because the Circuit Court of Talladega County expressly found that its decision was final and that there was no reason for delay, its July 7, 1994, order was immediately appealable and thus would be accorded preclusive effect under Alabama law as of that date.

DAI urges this court nevertheless to disregard the Alabama judgment, for three reasons. First, DAI argues that the Supreme Court's decision in *Allied-Bruce Terminix Cos. v. Dobson*, 115 S. Ct. 834 (1995), overturned the interstate commerce analysis that provided the Alabama court's fourth rationale for voiding the arbitration clause. The Supreme Court's decision, DAI contends, constitutes an "intervening change in the applicable legal context," *Staten Island Rapid Transit Operating Auth. v. ICC*, 718 F.2d 533, 543 (2d Cir. 1983), that requires a federal court not to accord preclusive effect to the Alabama decision. *See* RESTATEMENT (SECOND) OF JUDGMENTS § 28(2) (1980). Even if *Allied-Bruce* did undermine one rationale supporting the Alabama court's judgment, however, the Supreme Court's decision did not affect the alternate grounds set forth by the court for voiding the arbitration clause. Because the legal context has not shifted at all in these other areas, we cannot reexamine the Alabama judgment.

Second, DAI contends that it was not afforded a "full and fair opportunity to litigate" the arbitration claims in the Alabama court. *See Milltex Indus. Corp. v. Jacquard Lace Co.*, 922 F.2d 164, 168 (2d Cir. 1991); *Stone*, 970 F.2d at 1056. DAI assigns error to three aspects of the procedure followed in the Alabama court, each of which we reject. (1) DAI complains that it was not afforded the right to file a brief in response to McCrary's "Motion to Determine the Non-Arbitrability of the Issues." But as DAI conceded at oral argument before this court, nothing in the record indicates that it ever sought to file such a brief, much less that the Alabama court prevented it from filing one. Absent any evidence to the contrary, we accept the statement in the written order of the Alabama court that "[b]oth sides have thoroughly briefed the issues and provided factual evidence in support of their respective positions." (2) DAI also claims that it was not afforded "meaningful oral argument." Because DAI does not claim that oral argument was completely denied, we dismiss the argument out of hand. This court has held that "[o]ral argument is not a necessary component of due process in all circumstances." *Zaluski v. INS*, 37 F.3d 72, 73 (2d Cir. 1994); *see also FCC v. WJR, The Goodwill Station, Inc.*, 337 U.S. 265, 276 (1949) ("Certainly the Constitution does not require oral argument in all cases where only insubstantial or frivolous questions of law, or indeed even substantial ones, are raised."). Courts have broad discretion to determine how much, if any, oral argument is appropriate in a given case. We will not second-guess the Alabama court's allocation of its time. (3) Finally, DAI argues that the Alabama court drastically misapplied the law. This argument is nothing more than an invitation for this court to revisit the merits of the Alabama court's judgment--precisely what the full faith and credit statute tells us not to do. *See Charles Koen & Assocs. v. City of Cairo*, 909 F.2d 992, 1000 n.8 (7th Cir. 1990) ("The full faith and credit statute does not permit federal courts to reassess the merits of state court judgments."). "Lower federal courts are not superior to state courts." *Lion Bonding & Sur. Co. v. Karatz*, 262 U.S. 77, 90 (1923); *see also District of Columbia Court of Appeals v. Feldman*, 460 U.S. 462, 482

(1983) ("[A] United States District Court has no authority to review final judgments of a state court in judicial proceedings."). If DAI is dissatisfied with the judgment of the Alabama trial court, it should take an appeal.

Third, DAI argues that there was no motion properly before the Alabama court that would permit it to decide the arbitrability issue. That is, DAI claims that it had already withdrawn its own motion to compel arbitration under § 3 of the FAA, and that McCrary's own "Motion to Determine the Non-Arbitrability of the Issues" was unauthorized, considering that McCrary had never sought a declaratory judgment in his complaint. According to DAI, the Alabama opinion is therefore purely "advisory," and is not entitled to preclusive effect under state law. This argument fails for two reasons. First, the Alabama court clearly believed that DAI's motion to dismiss had been submitted for decision, since it denied that motion on the merits. Second, *Stamps v. Jefferson County Board of Education*, 642 So. 2d 941, 944 (Ala. 1994), which DAI cites, does not support the proposition that a declaratory judgment is merely "advisory" if such relief was not specifically requested in the complaint. All the Alabama Supreme Court stated in *Stamps* was that "[a]ctions or opinions are denominated 'advisory,'. . . where the judgment sought would not constitute specific relief to a litigant . . . ." 642 So. 2d at 944 (quoting EDWIN M. BORCHARD, DECLARATORY JUDGMENTS 34 (1934)) (emphasis deleted). In that case, a group of teachers had sued their employer and sought a judicial declaration that their work duties subjected them to prosecution by a state agency. The court held that such a declaratory judgment would be purely advisory because the prosecutorial agency had not been joined as a party, and thus would not be bound by the decision. *Id.* But DAI is a party in the Alabama action, and is bound by the state court judgment. Because the declaratory judgment finding the arbitration clause to be unenforceable provides "specific relief" to McCrary against DAI, as required by *Stamps*, it cannot be brushed aside as an "advisory" opinion.

For these reasons, we hold that the district court should have accorded full faith and credit to the Alabama judgment.

Accordingly, we reverse the district court orders denying McCrary's motion to dismiss and compelling him to pursue arbitration. On remand, we direct the district court to dismiss DAI's petition to compel McCrary to arbitrate. Although McCrary did not appeal from the December 9, 1994 order entering the preliminary injunction, we nevertheless exercise our pendent appellate jurisdiction in the interests of judicial economy to vacate the injunction. *See Golino v. City of New Haven*, 950 F.2d 864, 868 (2d Cir. 1991) ("[W]here we have jurisdiction to consider some questions on appeal, we may exercise our discretion to take pendent jurisdiction over related questions."), *cert. denied sub nom. Lillis v. Golino*, 112 S. Ct. 3032 (1992).

### 2. *The Illinois Judgments (Cases ## 1-6, 15-16, DAI v. Bickel)*

Eight groups of Illinois franchisees[7] filed complaints against DAI, its leasing companies, and DAI's two co-owners, and their cases were eventually consolidated before the Circuit Court of Madison County, Illinois. On October 24, 1994, the Illinois court granted the franchisees' motion for summary judgment, declaring the arbitration clause void and unenforceable on several grounds. The court stated that its decision was a "final and appealable order and judgment under Illinois Supreme Court Rule 304(a) in that there is no just reason for delaying either the enforcement of or the appeal from this judgment and order."

DAI represented to the district court that it had filed a motion for reconsideration in the Illinois court, and that the possibility of appeal remained open. Reasoning that a judgment subject to appeal was not final under Illinois law, the district court refused to accord preclusive effect to the Illinois court's decision. The district court relied on *Pelon v. Wall*, 262 Ill. App. 3d 131, 135 (2d Dist. 1994), which held that "[f]or res

---

[7] Cases 1, 2, 3, 4, 5, 6, 15, 16, and *DAI v. Bickel*. *See supra* note 2 for the list of franchisees involved in each case listed here.

judicata purposes, a judgment is not final until the possibility of appellate review has been exhausted."

The Bickels also filed a complaint against DAI and others in the Circuit Court of Madison County, on December 16, 1994. DAI failed to enter an appearance in Madison County within the prescribed time, so the Illinois court entered a default judgment in favor of the Bickels on February 7, 1994. In its judgment, the Illinois court declared the arbitration clause void and unenforceable, and scheduled a hearing on damages for April 4, 1995. On February 13, 1995, however, the district court ruled that for the purposes of issue preclusion, the Illinois judgment obtained by the Bickels was no more final than the judgment obtained by the other franchisees in Madison County. Accordingly, the district court granted DAI's petition to compel arbitration and enjoined the Bickels from continuing their Illinois litigation. The injunction contained an exception, however, which permitted DAI to move the Illinois court to set aside its default judgment.

The Illinois Supreme Court has held that an Illinois judgment is not final, and thus not entitled to preclusive effect, until the time for appeal has expired. *Bellweg v. City of Springfield*, 114 Ill. 2d 107, 113 (1985) ("For purposes of applying the doctrine of collateral estoppel, finality requires that the potential for appellate review must have been exhausted."); *Relph v. Board of Educ.*, 84 Ill. 2d 436, 442 (1981) (holding that an appellate court's mandate to remand with instructions for further proceedings establishes the law of the case, but does not constitute a final judgment entitled to res judicata effect--partially because the trial court's further proceedings are subject to subsequent appeal, and partially because the appellate court's mandate is subject to review by the Illinois Supreme Court); *see also People v. Condon*, 246 Ill. App. 3d 74, 76 (2d Dist. 1993) (holding that judgment is not final for purposes of preclusion until the potential for appellate review has been exhausted).

The franchisees respond by citing *Illinois Founders Insurance Co. v. Guidish*, 248 Ill. App. 3d 116, 120 (1st Dist. 1993), where it was said that

> [t]he pendency of an appeal has no effect on the finality of the order appealed from. Under certain circumstances, the pendency of an appeal can affect the enforceability of a judgment . . . but not its finality. More to the point, a final judgment can serve as the basis to apply the doctrines of res judicata and collateral estoppel even though the judgement is being appealed.

The Illinois Appellate Court's statement in *Guidish* is clearly at odds with the Illinois Supreme Court's categorical statements in *Bellweg* and *Relph*. *See Prymer v. Ogden*, 29 F.3d 1208, 1213 n.2 (7th Cir.) (discussing, but declining to resolve, conflict in authority), *cert. denied*, 115 S. Ct. 665 (1994). Despite the best efforts of the franchisees to distinguish *Bellweg* and *Relph*, we must follow the rulings of the Illinois Supreme Court.[8]

We hold that the district court correctly refused to accord preclusive effect to the Illinois judgments.

### 3. *North Carolina (Case #7)*

In April 1993, Michael Johnson filed a complaint against DAI and several affiliated individuals in the General Court of Justice, Superior Court Division, in Gaston County, North Carolina. Johnson alleged, *inter alia*, fraud, breach of contract, and conversion. DAI replied by filing two motions. First, it moved to stay the lawsuit pending arbitration. Second, it moved to dismiss Johnson's complaint, on the grounds that he had waived his right to challenge the arbitration agreement by previously participating in arbitration proceedings with DAI. Johnson, in turn, claimed that the arbitration clause was unenforceable on several grounds, including (1) that it lacked mutuality and (2) that he had been fraudulently induced into executing the arbitration agreement.

---

[8] We note that many of the franchisees' arguments were espoused in a *dissenting opinion* by a judge on the Illinois Appellate Court, who directly criticized the holding of *Bellweg* for deviating from the Restatement (Second) of Judgments § 13. *Southeastern Ill. Elec. Coop., Inc. v. Illinois Human Rights Comm'n*, 162 Ill. App. 3d 806, 814 (5th Dist. 1987) (Karns, J., dissenting), *appeal denied*, 119 Ill. 2d 575 (1988).

On May 3, 1994, the North Carolina court denied both of DAI's motions. In its written order, the court explicitly addressed only the issues raised in DAI's motion to dismiss: it held that Johnson's "limited participation in the arbitration proceedings did not constitute a waiver of his right to challenge the enforceability of the arbitration clause." With respect to DAI's *first motion*, however, the court did not explain why it denied the stay, nor did it make any findings of fact or conclusions of law regarding the arbitration clause.

Johnson argues that the North Carolina court *must* have relied on one of the rationales offered by Johnson (lack of mutuality or fraudulent inducement) even though the court did not specify which one. In North Carolina, however, collateral estoppel only precludes the relitigation of issues that were actually and necessarily decided in the earlier action. *King v. Grindstaff*, 200 S.E.2d 799, 805 (N.C. 1973). The party invoking the benefit of collateral estoppel (here, Johnson) bears the burden of establishing what was in fact determined by the prior judgment. *Thomas M. McInnis & Assocs., Inc. v. Hall*, 349 S.E.2d 552, 557 (N.C. 1986). Even if one of the issues raised by Johnson--mutuality or fraudulent inducement--was *necessarily* decided by the state judge, it is impossible to ascertain which issue was *actually* decided. We therefore hold that the judgment of the Gaston County court would not be accorded preclusive effect under North Carolina law with respect to the validity of the arbitration clause.

Accordingly, we affirm the district court's decision not to accord full faith and credit to the judgment against DAI obtained by Johnson in the North Carolina court.[9]

---

[9] The district court refused to give full faith and credit to the North Carolina judgment on the grounds that it was subject to appeal, and thus did not constitute a final order entitled to preclusive effect. On appeal before this court, DAI concedes and we agree that the North Carolina judgment is a "final" order for the purposes of North Carolina preclusion law. *Sims v. Ritter Constr., Inc.*, 62 N.C. App. 52, 55, 302 S.E.2d 293, 295 (1983) (holding that interlocutory order affecting a substantial right is final and appealable, and entitled to *res judicata* effect under North Carolina law).

### C. *The Franchisees' Challenges to the Arbitration Clause*

#### 1. *Mutuality*

The franchisees argue that the arbitration clause is void for lack of mutuality, in that it requires a franchisee to submit all controversies to arbitration but reserves to DAI (through its leasing companies) the right to seek summary eviction against the franchisees. The district court rejected this argument, finding no lack of mutuality: If the leasing companies were separable entities, then "the arbitration clause will be enforceable only as to DAI and the [franchisees], obliging them to arbitrate, thus establishing mutuality." If, on the other hand, the leasing companies were indistinguishable from DAI, then they too would be bound to arbitrate. Either way, the court reasoned, mutuality was not an issue.

We agree that mutuality is not an issue, but for different reasons. Preliminarily, we note that the parties have not offered any reason why we should not apply the choice-of-law clause in the franchise agreements, which indicates that Connecticut law applies. Connecticut courts, however, have not addressed the precise question whether an arbitration clause may be void for "lack of mutuality."

The term "mutuality" can refer to several different concepts in contract law. Although it is unclear whether the franchisees are referring to "mutuality of obligation" or "mutuality of remedy," both doctrines are largely dead letters. The doctrine of "mutuality of obligation" requires a valid contract to be based on an exchange of reciprocal promises. 1A ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 152, at 3 (1963). As applied to arbitration clauses, that rule has been restated to mean that "the consideration exchanged for one party's promise to arbitrate must be the other party's promise to arbitrate." *Hull v. Norcom, Inc.*, 750 F.2d 1547, 1550 (11th Cir. 1985) (interpreting New York law). But "mutuality of obligation" has been largely rejected as a general principle in contract law, as well as in the arbitration context. The latest Restatement of Contracts provides that "[i]f the requirement

of consideration is met, there is no additional requirement of . . . 'mutuality of obligation.'" RESTATEMENT (SECOND) OF CONTRACTS § 79 (1979). Option contracts, for example, are unquestionably valid under this modern rule despite their lack of "mutuality of obligation." That is, one party's promise to honor a future offer to purchase an item is valid if supported by the other party's present payment of a sum of money. The promise to *accept* the offer need not be supported by a reciprocal promise to *make* that offer. The New York Court of Appeals essentially adopted the Second Restatement position in a case involving a challenge to an arbitration clause which bound only one of the parties to arbitrate. In *Sablosky v. Edward S. Gordon Co.*, 73 N.Y.2d 133, 137, 538 N.Y.S.2d 513, 516 (1989), the court held that

> [i]f there is consideration for the entire agreement that is sufficient; the consideration supports the arbitration option, as it does every other obligation in the agreement. . . . Since it is settled that the validity of an arbitration agreement is to be determined by the law applicable to contracts generally . . . there is no reason for a different mutuality rule in arbitration cases.

Most courts facing this issue have arrived at the same conclusion. *See, e.g., Wilson Elec. Contractors, Inc. v. Minnotte Contracting Corp.*, 878 F.2d 167, 168 (6th Cir. 1989); *Becker Autoradio U.S.A., Inc. v. Becker Autoradiowerk GmbH*, 585 F.2d 39, 47 (3d Cir. 1978); *W.L. Jorden & Co. v. Blythe Indus.*, 702 F. Supp. 282, 284 (N.D. Ga. 1988); *Willis Flooring, Inc. v. Howard S. Lease Constr. Co. & Assocs.*, 656 P.2d 1184, 1185 (Alaska 1983) ("As one clause in a larger contract, the [arbitration] clause is binding to the same extent that the contract as a whole is binding."); *LaBonte Precision, Inc. v. LPI Indus. Corp.*, 507 So. 2d 1202, 1203 (Fla. Dist. Ct. App. 1987); *Kalman Floor Co. v. Jos. L. Muscarelle, Inc.*, 196 N.J. Super. 16, 481 A.2d 553 (1984), *aff'd for reasons stated below*, 98 N.J. 266, 486 A.2d 334 (1985). *Contra Stevens/Leinweber/Sullens, Inc. v. Holm Dev. & Management, Inc.*, 795 P.2d 1308, 1313 (Ariz. Ct. App. 1990); *R.W.*

*Roberts Constr. Co. v. St. Johns River Water Management Dist.*, 423 So. 2d 630, 633 (Fla. Dist. Ct. App. 1982).

It has been argued that, according to the Supreme Court's decision in *Prima Paint Corp. v. Flood & Conklin Manufacturing Co.*, 388 U.S. 395, 403-04 (1967), an arbitration clause is separable from its underlying contract, and therefore must be supported by separate consideration. *Stevens*, 795 P.2d at 1312-13. In *Prima Paint*, the Court held that a claim of fraud in the inducement of an underlying contract must be left to the arbitrators, but that a claim of fraud in the inducement of the arbitration clause should be decided by the court. *Prima Paint*, 388 U.S. at 403-04. In reaching this conclusion, the Court endorsed the result reached by our court in *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402 (2d Cir. 1959) (Medina, J.), *cert. granted*, 362 U.S. 909, *cert. dismissed for mootness*, 364 U.S. 801 (1960).[10] In *Robert Lawrence*, we described the FAA as distinguishing between "the entire contract between the parties on the one hand and the arbitration clause of the contract on the other," 271 F.2d at 409--the latter being described as a "separable part of the contract." *Id.* at 410. At one point in *Robert Lawrence*, we speculated that

> we would suppose that generally where the arbitration provision of the contract is sufficiently broad to encompass the issue of fraud, the mutual promises to arbitrate would form the *quid pro quo* of one another and constitute a separable and enforceable part of the agreement. We do not decide this point, however, as it is not necessarily before us.

*Id.* at 411. This passage, one might argue, indicates that an arbitration clause must be treated as a contract supported by independent consideration. For the following reasons, however, we reject this characterization.

---

[10] *Prima Paint*, 388 U.S. at 400 ("We agree [with the result reached in *Robert Lawrence*], albeit for somewhat different reasons. . . .")

First, of course, we clearly labelled our statement in *Robert Lawrence* as dicta. Second, though we suggested that mutual promises to arbitrate could constitute sufficient consideration to support an arbitration agreement, we did not exclude the possibility that other consideration could support the agreement. Third, we indicated only that arbitration clauses are "separable" from void or voidable provisions of a contract--not that they are independent contracts. Although we consider an arbitration clause separately for the limited purpose of evaluating a claim of fraudulent inducement, we do not do so for all purposes. For example, when determining the parties' intent in the arbitration clause, we must read the contract as a whole. *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 115 S. Ct. 1212, 1217 (1995) (quoting RESTATEMENT (SECOND) OF CONTRACTS. § 202(2) (1979)). State law generally governs the determination of whether the parties agreed to arbitrate a certain matter, *First Options of Chicago, Inc. v. Kaplan*, 115 S. Ct. 1920, 1924 (1995), and Connecticut courts "construe the contract as a whole" and consider "all relevant provisions . . . when determining the intent of the parties." *White v. Kampner*, 641 A.2d 1381, 1385 (Conn. 1994).

*Wilson Electrical Contractors, Inc. v. Minnotte Contracting Corp.*, 878 F.2d 167, 169 (6th Cir. 1989), rejected the contention that under *Prima Paint*, "an arbitration clause is an independent contract that is separable from the main contract in which it is found and therefore must have all of the essential elements of a contract, including consideration." As the *Wilson* court pointed out, more recent decisions of the Supreme Court have consistently emphasized that the FAA is grounded in a strong federal policy favoring arbitration. *Id.* at 169. A doctrine that required separate consideration for arbitration clauses might risk running afoul of that policy. In any event, because the franchisees make no claim that the underlying contract was the result of fraud, we have no occasion to consider the arbitration clause in isolation from the larger contract. Accordingly, we need not decide whether the arbitration clause must be supported by independent consideration.

The doctrine of "mutuality of remedy" affords no greater relief for the franchisees. That rule, which provides generally that a "plaintiff shall not get specific enforcement unless the defendant could also have obtained it," 5A ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1181, at 336 (1964), is also defunct. *See, e.g., Sablosky*, 73 N.Y.2d at 137 ("Mutuality of remedy is not required in arbitration contracts."). As explained in the latest Restatement,

> the law does not require that the parties have similar remedies in case of breach, and the fact that specific performance or an injunction is not available to one party is not a sufficient reason for refusing it to the other party. The rationale of the supposed requirement of "mutuality of remedy" is to make sure that the party in breach will not be compelled to perform without being assured that he will receive any remaining part of the agreed exchange from the injured party. It is therefore enough if adequate security can be furnished.

RESTATEMENT (SECOND) OF CONTRACTS § 363 cmt. c (1979).

In view of Connecticut's strong policies favoring arbitration, *see, e.g., White v. Kampner*, 229 Conn. 465, 471, 641 A.2d 1381, 1384 (1994); *Garrity v. McCaskey*, 223 Conn. 1, 7, 612 A.2d 742, 746 (1992), we believe that the Connecticut courts would conclude that "where the agreement to arbitrate is integrated into a larger unitary contract, the consideration for the contract as a whole covers the arbitration clause as well." *W.L. Jorden & Co.*, 702 F. Supp. at 284. The franchisees do not contest that the franchise agreement as a whole is supported by consideration. Absent a failure of consideration, in this instance, we cannot invalidate the agreement in whole or in part.

### 2. *Waiver of Right to Pursue Arbitration*

The district court held that regardless of whether the leasing companies were DAI's alter egos, DAI had not waived its

right to compel arbitration under the franchise agreement. On the one hand, if the leasing companies were not DAI's alter egos, then their pursuit of eviction proceedings against the franchisees could not be imputed to DAI. On the other hand, even if the leasing companies were DAI's alter egos, DAI nevertheless invoked its arbitration rights as soon as it was named a party in the various state court actions commenced by the franchisees. Somewhat opaquely, the court held that DAI "cannot be held to have waived a right of arbitration by an after-the-fact holding that it is the alter ego of the leasing companies." We disagree.

There is no authority to support the notion that a party is liable for acts of its alter ego only if a court has previously found that an alter-ego relationship exists. As we have explained in the context of contractual liability, "it is clear that the consequence of applying the alter ego doctrine is that the corporation and those who have controlled it without regard to its separate entity are treated as but one entity, and . . . the acts of one are the acts of all." *Fisser v. International Bank*, 282 F.2d 231, 234 (2d Cir. 1960) (holding parent corporation bound to arbitrate, where its alter-ego instrumentality signed arbitration agreement); *see also Interocean Shipping Co. v. National Shipping & Trading Corp.*, 523 F.2d 527, 539 (2d Cir. 1975) (holding that company may be compelled to arbitrate even if not party to agreement containing arbitration clause, where company is alter ego of another party that clearly is subject to arbitration), *cert. denied*, 423 U.S. 1054 (1976). We believe that this principle applies with equal force in the present context. If DAI and its leasing companies should be treated as one and the same, then the initiation of eviction proceedings by the leasing companies must be imputed to DAI.

There remain two further questions: (1) whether the district court or the arbitrators should determine the waiver issue, and (2) what standard should be used by the appropriate decisionmaker. As to the first question, we note that the defense of waiver is generally referable to the arbitrators in cases involving petitions to compel under § 4 of the FAA--with one

important exception which we shall shortly explain. In *World Brilliance Corp. v. Bethlehem Steel Co.*, 342 F.2d 362 (2d Cir. 1965), we squarely held that issues of waiver, like issues of fraud in the inducement of the entire contract, were properly resolved by the arbitrators, not the district court. *Id.* at 364-65. In reaching this conclusion, we pointed out that § 2 of the FAA makes an arbitration agreement enforceable "'save upon such grounds as exist at law or in equity for the revocation of any contract.'" *Id.* at 364 (quoting 9 U.S.C. § 2). Waiver, we explained, does not constitute a ground for "revocation" of a contract within the meaning of § 2, and thus is not a basis for invalidating an arbitration contract. *Id.* Likewise, we explained that under § 4, a court is required to grant a petition to compel arbitration except where a question of fact exists as to (1) "the making of the arbitration agreement" or (2) the "failure, neglect, or refusal of *another* [i.e., the respondent to the § 4 petition] to arbitrate." *Id.* at 364-65 (quoting 9 U.S.C. § 4 (emphasis added)). Because acts *by the petitioner* constituting waiver of the right to arbitrate did not fall within either of these enumerated categories, a district court cannot refuse to order arbitration under § 4 on a theory of waiver. *Id.* at 365. We reaffirmed this restrictive interpretation of § 4 in *Trafalgar Shipping Co. v. International Milling Co.*, 401 F.2d 568, 571 (2d Cir. 1968), where we held that most questions regarding the defense of laches should be decided "by the arbitrators, not the courts." In that case, we repeated that "[t]he only issues which the court is authorized to consider on a motion to compel arbitration are ones which pertain to 'the making of the arbitration agreement or the failure, neglect, or refusal to perform the same,'" *id.* at 571, and that the latter phrase referred to the failure of the *respondent* in a § 4 action to submit to arbitration, *id.* at 572.

Our decision in *World Brilliance* did not call into question, however, a parallel line of cases that considers waiver to be an equitable defense to a stay application under § 3 of the FAA, which a court is empowered to consider. Section 3 authorizes a court to stay proceedings pending arbitration, "providing the applicant for the stay is not in default in proceeding with such arbitration." 9 U.S.C. § 3. For example, in *Kulukundis*

*Shipping Co. v. Amtorg Trading Corp.*, 126 F.2d 978 (2d Cir. 1942), a defendant sought to amend his answer nine months into the litigation and two months before trial, raising for the first time the defense that the case was arbitrable. *Id.* at 986. We construed the defendant's motion to amend as an application for a § 3 stay of proceedings. *Id.* at 986 n.29. We explained that the proviso in § 3--that a stay shall be granted "providing the applicant for the stay is not in default in proceeding with such arbitration"--referred to a party "who, when requested, has refused to go to arbitration or who has refused to proceed with the hearing before the arbitrators once it has commenced." *Id.* at 989. We also noted with approval that, in other courts,

> [a] plaintiff who brought suit on a contract, without seeking to avail himself of its arbitration clause, has been held to have waived his rights thereunder, so that he could not subsequently, after a long delay, ask the court, under Section 3, to stay the action pending arbitration.

*Id.* We also indicated our agreement with a Fourth Circuit decision finding waiver of the right to arbitrate by a counterclaim defendant who participated at length in litigation, but on the eve of trial moved for a stay under § 3 of the FAA. *Id.* (describing *Radiator Specialty Co. v. Cannon Mills, Inc.*, 97 F.2d 318 (4th Cir. 1938)). The defendant in *Kulukundis* did not waive its right to arbitrate, we held, because it had not pursued litigation as extensively as had the parties in these other cases. 126 F.2d at 989.

We again equated a waiver of the right to arbitrate with a "default in proceeding with such arbitration" under § 3 in *Robert Lawrence*, 271 F.2d at 412; *see Carcich v. Rederi A/B Nordie*, 389 F.2d 692, 696 (2d Cir. 1968) (deciding waiver issue where defendant moved for stay). The Court of Appeals for the District of Columbia Circuit apparently took the same view, when it explained that

> [t]he right to arbitration, like any other contract right, can be waived. A party waives his right to arbitrate

> when he actively participates in a lawsuit or takes other action inconsistent with that right. Once having waived the right to arbitrate, that party is necessarily "in default in proceeding with such arbitration."

*Cornell & Co. v. Barber & Ross Co.*, 360 F.2d 512, 513 (D.C. Cir. 1966) (per curiam).

Yet some of our cases have also recognized that a court may consider a waiver defense to § 4 actions to compel arbitration as well as to § 3 stay applications--seemingly in derogation of our holding in *World Brilliance*. For example, in *Chatham Shipping Co. v. Fertex Steamship Corp.*, 352 F.2d 291, 293-94 (2d Cir. 1965), the petitioner had filed a complaint alleging breach of a contract but then filed a § 4 petition and moved to dismiss the first complaint, before the defendant had even filed an answer. We rejected the respondent's defense of waiver on the merits, even though *World Brilliance* had been decided only seven months earlier. In *Demsey & Associates, Inc. v. S.S. Sea Star*, 461 F.2d 1009, 1017 (2d Cir. 1972), where a defendant in a contract action pleaded arbitration "as an affirmative defense" after trial had been completed, we did not construe it as seeking either a § 3 stay or a § 4 order compelling arbitration. We held that the defendant's failure to raise the arbitration issue until after filing cross-claims, participating in discovery, and going to trial on the merits constituted waiver of its right to arbitrate. *Id.* The court did not discuss its authority for reaching the waiver issue--possibly because the defendant had neither sought a stay under § 3, nor petitioned the court to compel arbitration under § 4. *Id.* Yet in all of the cases cited in *Demsey*, except *Chatham*, the court decided the waiver issue only where a defendant, deep into the litigation, sought a stay of judicial proceedings under § 3 of the FAA. *Id.* at 1017-18.[11]

---

[11] *Demsey* cited the following cases: *Carcich v. Rederi A/B Nordie*, 389 F.2d 692 (2d Cir. 1968) (holding no waiver where defendant moved for § 3 stay after participating in discovery and pretrial conferences); *Robert Lawrence*, 271 F.2d 402 (holding no waiver where defendant moved for

*(Footnote continued)*

Any distinction between § 3 and § 4 actions--never fully explicated--submerged even more deeply by the time this court decided *Sweater Bee by Banff, Ltd. v. Manhattan Industries, Inc.*, 754 F.2d 457 (2d Cir.), *cert. denied*, 474 U.S. 819 (1985). That case involved a defendant who, only after obtaining an adverse ruling on a motion to dismiss pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure, sought both a § 3 stay and a § 4 order compelling arbitration. 754 F.2d at 459. Citing *Demsey*, we stated that "[t]he rule of this circuit . . . is that the litigation of substantial issues going to the merits may constitute a waiver of arbitration," *id.* at 461, and proceeded to decide the waiver issue. Shortly thereafter, we faced a similar case involving a defendant who sought to sever certain claims from ongoing litigation and petitioned the court to compel arbitration of those claims under § 4 of the FAA. *Rush v. Oppenheimer & Co.*, 779 F.2d 885, 886 (2d Cir. 1985). We made it clear that "waiver of the right to compel arbitration due to participation in litigation may be found only when prejudice to the other party is demonstrated," *id.* at 887, and again decided the waiver issue. Finally, in *Kramer v. Hammond*, 943 F.2d 176 (2d Cir. 1991), we held that a party bringing a petition to compel under § 4 had waived his right to arbitration by engaging in prior litigation in state courts, not in the district court.[12] *Id.* at 180. Again, the parties did not

---

§ 3 stay in the answer); *Reynolds Jamaica Mines, Ltd. v. La Societe Navale Caennaise*, 239 F.2d 689 (4th Cir. 1956) (in what was arguably a § 3 action, finding no waiver and dismissing federal lawsuit because dispute was arbitrable--but not ordering arbitration); *Hilti Inc. v. Oldach*, 392 F.2d 368 (1st Cir. 1968) (holding no waiver where defendant moved for § 3 stay eight months after raising arbitrability as a defense in answer); *Mason v. Stevensville Golf & Country Club, Inc.*, 292 F. Supp. 348 (S.D.N.Y. 1968) (Pollack, J.) (finding no waiver where defendant sought § 3 stay after failing to object to scheduling of trial).

[12] Prior to our decision in *Kramer*, all of the cases in which we reached the issue of waiver involved substantial litigation on the merits in the district court which was asked to grant the § 3 stay, not in other state or federal courts. Our decisions to rule on the waiver issue, rather than to refer the question to the arbitrators, could have been explained as exercises of the federal courts' inherent power to deal with abusive litigation practices in

*(Footnote continued)*

raise and we did not discuss why this issue was for the courts rather than the arbitrators to resolve.

It would appear that the waiver defense has slowly been transformed from a statutorily mandated inquiry in § 3 cases--whether the "applicant for the stay is . . . in default in proceeding with such arbitration"--into a broader equitable defense in § 4 cases. This trend has its limits, however, and another of our decisions suggests how the equitable waiver defense may be reconciled with our holdings in *World Brilliance*. In *Prudential Lines, Inc. v. Exxon Corp.*, 704 F.2d 59 (2d Cir. 1983), we reaffirmed the holdings of *World Brilliance* and *Trafalgar* that a waiver defense, like a laches defense, was "an arbitrable issue." *Id.* at 67. We noted that in the cases where the court itself decided the issue of waiver, the "party had previously participated in court proceedings to litigate the same dispute." *Id.* at 67 n.8. We therefore distinguished between cases where the waiver defense was based on prior litigation by the party seeking arbitration--when the court should decide the issue of waiver--and those when the defense was based on other actions. It may be that the modern evolution of our waiver

---

their courtrooms. *See, e.g., Chambers v. Nasco*, 501 U.S. 32, 44-45 (1991) ("A primary aspect of [a court's] discretion [to exercise its inherent powers] is the ability to fashion an appropriate sanction for conduct which abuses the judicial process."); *Link v. Wabash R.R.*, 370 U.S. 626, 629 (1962) ("The authority of a federal trial court to dismiss a plaintiff's action with prejudice because of his failure to prosecute cannot seriously be doubted.") *Landis v. North Am. Co.*, 9 U.S. 248, 254 (1936) ("[T]he power to stay proceedings is incidental to the power inherent in every court to control the disposition of the causes on its docket with economy of time and effort for itself, for counsel, and for litigants."); *United States v. Hudson*, 7 Cranch 32, 34 (1812) (holding that the inherent powers of federal courts are those which "are necessary to the exercise of all others"). In *Kramer*, however, we reached the question of waiver even though the petitioner had not engaged in prior litigation in the district court. Our precedent therefore teaches that a court's ability to reach the question of waiver as a defense to arbitration is not grounded solely in its ability to control litigation practices before it. In light of *Kramer*, we are bound to hold that a district court may reach the question of waiver whenever a party seeking arbitration has engaged in any prior litigation.

doctrine does not correspond precisely to our understanding of the FAA thirty years ago. Yet we are bound to abide by our most recent precedent. *Cf. Commodity Futures Trading Commission v. Dunn*, 58 F.3d 50, 54 (2d Cir. 1995) (holding that a panel of Court of Appeals may not "disregard the reasoning of a decision [of a prior panel] because an entirely different line of reasoning was available").

Clearly, the present case falls squarely within the parameters of *Kramer v. Hammond*, where the party invoking arbitration (DAI) was allegedly involved in prior litigation in state courts. Pursuant to the distinction we drew in *Prudential Lines*, and consistent with *Kramer*, we hold that the issue of DAI's waiver of arbitration is for the district court to resolve on remand. To do so, the court must evaluate the franchisees' factual contentions, including whether the leasing companies were mere alter egos of DAI. If DAI was responsible for the eviction proceedings, the court must then determine whether prosecution of those eviction actions constituted litigation of "substantial issues going to the merits," *Sweater Bee*, 754 F.2d at 461. This inquiry will require a determination of whether, in fact, the particular eviction proceedings were based on the cross-default provisions of the subleases. If the alleged violations of the subleases were premised on violations of the franchise agreement (which DAI was contractually bound to resolve through arbitration) then DAI did litigate substantial issues going to the merits, and the only remaining question will be whether the franchisees suffered prejudice from the eviction proceedings. *See, e.g., Cotton v. Slone*, 4 F.3d 176 (2d Cir. 1993) (finding prejudice where defendant failed to pursue interlocutory appeal from denial of motion to compel, and instead fully litigated arbitrable issues on the merits in the district court); *Com-Tech Assocs. v. Computer Assocs. Int'l, Inc.*, 938 F.2d 1574, 1576-77 (2d Cir. 1991) (finding prejudice where defendant's extensive litigation before raising issue of arbitration forced plaintiffs to litigate arbitrable claims, and caused considerable expense and delay).

Accordingly, we reverse the district court's order rejecting the franchisees' waiver argument, and remand for further proceedings.

### 3. *Fraudulent Misrepresentation*

The franchisees argue that DAI fraudulently misrepresented to them that arbitration was a condition precedent to the institution of legal action by either party to the franchise agreement. They argue that DAI had, in reality, reserved the right to bring summary eviction actions against the franchisees through its leasing companies. The franchisees also claim that DAI failed to disclose that it had a custom and practice of bringing summary eviction proceedings and other legal proceedings for alleged violations of the franchise agreement. The district court held that these allegations would be pertinent only if the leasing companies[13] were indeed DAI's alter egos. Both the alter-ego and fraudulent-inducement issues, the court concluded, should properly be left to the arbitrators. This was error.

In *Prima Paint*, 388 U.S. at 403-04, the Supreme Court stated that "if the claim is fraud in the inducement of the arbitration clause itself--an issue which goes to the 'making' of the agreement to arbitrate--the federal court may proceed to adjudicate it." *See also Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 519 n.14 (1974) (citing *Prima Paint* for the proposition that "an arbitration or forum-selection clause in a contract is not enforceable if the *inclusion of that clause in the contract* was the product of fraud or coercion"). As this court has explained, if the "arbitration clause was induced by fraud, there can be no arbitration; and if the party charging this fraud shows there is substance to his charge, *there must be a*

---

[13] Although the district court actually referred to the "development agents" as being possible alter egos of DAI, it seems to have meant the "leasing companies." The franchisees do not allege that DAI's various development agents (who engaged in some negotiations on behalf of DAI with the franchisees) were DAI's alter egos.

*judicial trial of that question* before a stay can issue." *Robert Lawrence*, 271 F.2d at 411.

The franchisees allege that they were fraudulently induced to assent to the arbitration clause--not to the rest of the contract. Accordingly, under *Prima Paint*, the district court had to reach the fraudulent inducement issue before deciding whether to compel arbitration. Resolution of the fraud issue, in turn, will require an answer to the antecedent question of whether the leasing companies were DAI's alter egos.

We therefore reverse the district court's determination that the arbitrators rather than the court should decide the alter-ego and fraudulent-inducement questions. On remand, the district court must resolve these issues.

## III. CONCLUSION

To summarize:[14]

1. We affirm the district court's decision that it had subject matter jurisdiction over all of DAI's petitions to compel arbitration, because there was complete diversity between the parties to the arbitration clause.

2. We reverse the district court's holding that the Alabama court's judgment in the *McCrary* case (Case # 8) was not entitled to full faith and credit. That judgment had preclusive effect under Alabama law, and thus barred DAI from seeking to enforce its arbitration agreement with McCrary. We therefore reverse the district court's denial of franchisee McCrary's motion to dismiss DAI's motion to compel and its order granting DAI's petition to compel McCrary to arbitrate. In the exercise of our pendent appellate jurisdiction, we vacate the preliminary injunction barring McCrary from pursuing his Alabama state court claims against DAI. We direct the district court, on remand, to dismiss with prejudice DAI's motion to compel McCrary to arbitrate.

---

[14] For the list of cases affected by our ruling, *see supra* note 2.

3. We affirm the district court's holding that the Illinois courts' judgments in Cases ## 1-6, 15-16, and *DAI v. Bickel* were still subject to appeal, and thus under Illinois law were not entitled to preclusive effect. We therefore affirm the district court's denial of those franchisees' motions to dismiss.

4. We affirm the district court's holding that the North Carolina judgment in the *Johnson* case (Case # 7) was not entitled to full faith and credit. That judgment would not be accorded preclusive effect under North Carolina law, because the court's written order does not indicate what issues were actually decided. We therefore affirm the district court's denial of the Johnson franchisees' motion to dismiss.

5. We affirm the district court's holding that "mutuality" was not at issue, but on different grounds. We hold that where consideration supports a contract as a whole, an arbitration clause in that contract is not void for lack of consideration.

6. We reverse the district court's holding that DAI did not waive its right to petition to compel arbitration, and remand for further proceedings. We hold that if the leasing companies were mere alter egos of DAI, their pursuit of eviction proceedings based on violations of the franchise agreements could constitute waiver of DAI's right to demand arbitration.

7. We reverse the district court's decision to defer to the arbitrators on the question of whether DAI fraudulently induced the franchisees to enter into the arbitration agreement. On remand, the district court must decide this issue.

8. Because the district court should have decided the alter-ego, waiver and fraudulent-inducement issues, we reverse its order granting DAI's motion to compel arbitration in all cases and remand for further proceedings. We also reverse its entry of preliminary injunctions against all of the franchisees --including, in the exercise of our pendent appellate jurisdiction and in the interests of judicial economy, the Alabama franchisees.

9. Finally, because we reverse the district court's orders entering the preliminary injunctions, we need not address the franchisees' contention that those orders violated the Anti-Injunction Act.

## APPENDIX B

[Filed September 28, 1995]

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

Nos. 1724, 1725, 1726, 1988 August Term, 1994

Docket Nos. 94-9207, 94-9293, 94-9209, 95-7183

DOCTOR'S ASSOCIATES, INC.,

*Plaintiff-Appellee*,

v.

EMILY DISTAJO, RENATO DISTAJO, CONSTANTINO LAMANDO, MILO LAMANDO, JOSE ALBERTO BRENES, ALVARO GUERRERO, MARIA T. GUERRERO, WESAM S. YOUMARAN, LINDA YOUMARAN, JULIE SHINO, JOHNSON SHINO, ALBERT YONAN, LEYLAH YONAN, LOUIS LOENNEKE, MARY ANN BOOKOUT, MICHAEL JOHNSON, DEBORAH A. KANE, GREGORY F. KANE, BRUNO GIANNINI, RONALD ROTHMUND, PATRICIA ROTHMUND, JOHN S. PAPALEO, JOHN A. McCRARY, JOHN GILLON, SONYA SMITH, PAUL RIISE, MELISSA RIISE, and RHONDA BENTON,

*Defendants-Appellants*.

and

DOCTOR'S ASSOCIATES, INC.,

*Plaintiff-Appellee*,

v.

RAYMOND BICKEL and SANDRA BICKEL,

*Defendants-Appellants*.

Present: MINER, LEVAL and CABRANES, *Circuit Judges*.

## ORDER

IT IS HEREBY ORDERED that the opinion filed on September 12, 1995, be amended as follows:

*Slip op. at 7162, line 30 from top*: Insert footnote 13 after "remand."

*Slip op. at 7162, bottom of page*: Insert "[13]By so holding, we do not purport to reach the question of *how* the district court should resolve this issue. The defendants' jury demands should be considered by the district court in the first instance."

*Slip op. at 7162, lines 30-31 from top*: Delete "To do so, the court must evaluate the franchisees'" and insert "The"

*Slip op. at 7162, line 32 from top*: Delete ", including" and insert "to be resolved include"

*Slip op. at 7162, line 34 from top*: Delete "the court must then determine" and insert "it must then be determined"

*Slip op. at 7164, line 4 from top*: Change footnote number from 13 to 14.

*Slip op. at 7164, bottom of page*: Change footnote number from 13 to 14.

*Slip op. at 7165, line 3 from top*: Insert footnote 15 after "questions."

*Slip op. at 7165, bottom of page*: Insert "[15]*See supra* note 13."

*Slip op. at 7165, line 6 from top*: Change footnote number from 14 to 16.

*Slip op. at 7165, bottom of page*: Change footnote number from 14 to 16.

IT IS SO ORDERED:

FOR THE COURT.

/s/ George Lange III, Clerk

## APPENDIX C

[Filed Sep. 29, 1994]

UNITED STATES DISTRICT COURT

DISTRICT OF CONNECTICUT

DOCTOR'S ASSOCIATES, INC. :

-vs- : Civil No. 3:94CV00349 (PCD)

EMILY DISTAJO, ET AL. :

## RULING ON PENDING MOTIONS

Plaintiff filed a petition to compel arbitration pursuant to the Federal Arbitration Act (FAA) 9 U.S.C. § 4, and subsequently an application for a Temporary Restraining Order and a Preliminary Injunction. Defendants have filed various motions to dismiss, to transfer, and for a hearing on the matter.

*BACKGROUND*

Plaintiff Doctor's Associates, Inc. (DAI) is the national franchisor of "Subway" sandwich shops, and is a Florida corporation. DAI entered into written franchise agreements with defendants, permitting them to operate a Subway restaurant. The agreements contain an arbitration clause (paragraph 10c) which reads as follows:

> Any controversy or claim arising out of or relating to this contract or the breach thereof shall be settled by Arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association at a hearing to be held in Bridgeport, Connecticut and judgment upon an award rendered by the Arbitrator(s) may be entered in any court having jurisdiction thereof. The commencement of arbitration proceedings by an aggrieved party to settle disputes arising out or relating to this contract is a condition precedent to the commencement of legal action by either party.

> The cost of such a proceeding will be borne equally by the parties.

Defendants have filed suit against plaintiff, affiliated individuals and entities in various state courts. Plaintiff demanded arbitration of defendants' claims by the American Arbitration Association in accordance with the arbitration clause. Defendants have refused to arbitrate, and therefore plaintiff petitions here for an order directing defendants to arbitrate. Plaintiff moved for a temporary restraining order and for a preliminary injunction to stay the state court proceedings until this court could rule on the petitions to compel arbitration. On September 13, 1994 a hearing was held as to whether a preliminary injunction should enter. The temporary restraining order has expired.

*DISCUSSION*

1) *Motions for a Hearing*

Plaintiff's motions for a hearing on the petition to compel arbitration and on the motions to dismiss are denied.

2) *Motions to Dismiss*

A motion to dismiss under Rule 12(b)(6) must be decided solely on the facts alleged. *Goldman v. Belden*, 754 F.2d 1059, 1065-66 (2d Cir. 1985). Such a motion should be granted only where no set of facts consistent with the allegations could be proven entitling plaintiffs to relief. *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957). The issue is not whether plaintiffs will prevail, but whether they should be afforded the opportunity to offer evidence to prove their claims. *Id.*

A) *Local Rule 9*

The motions to dismiss filed in 3:94cv00370 *Doctor's Associates v. Smith* (doc. #5) and 3:94cv00369 *Doctor's Associates v. Gillon* (doc. #7) are denied for failure to file an accompanying memorandum of law as required by Local Rule 9.

B) *Subject Matter Jurisdiction*

Several of the defendants claim that this court does not have jurisdiction over the subject matter of the action because there is not complete diversity, as certain development agents of DAI doing business in the same states that defendants reside must be joined as plaintiffs in the various actions.[1] However, they are not parties to the contract that is at issue in the instant action. "Fed.R. Civ.P. 19 does not require the joinder of parties merely because they played some part in the underlying events of a dispute, but only if such parties are necessary in order to grant complete relief or if they would be prejudiced by not being joined." *Argo Partners, Inc. v. Littlefield, Adams & Co.*, 1994 WL 320616 (S.D.N.Y.). "Under the Arbitration Act, an arbitration agreement must be enforced notwithstanding the presence of other persons who are parties to the underlying dispute but not to the arbitration

---

[1] Defendants in 3:94cv00515 *Doctor's Associates v. Youmaran*, 3:94cv00803 *Doctor's Associates v. Brenes*, 3:94cv00514 *Doctor's Associates v. Guerro*, 3:94cv00516 *Doctor's Associates v. Shino*, 3:94cv00517 *Doctor's Associates v. Loenneke*, 3:94cv00349 *Doctor's Associates v. Distajo*, 3:94cv01457 *Doctor's Associates v. Papaleo* and 3:94cv01456 *Doctor's Associates v. Rothmund* are residents of Illinois. They allege that Phil Mesi and Subway Development of Chicagoland, Inc., both development agents of DAI and residents of Illinois, are indispensable parties under Fed.R.Civ.P. 19(b). Defendants in 3:94cv00998 *Doctor's Associates v. Kane* are residents of Massachusetts. They allege that Michael and Jane Eslinger and Jams, Inc., development agents of DAI and residents of Massachusetts, are indispensable parties. Defendant in 3:94cv00803 *Doctor's Associates v. Johnson* is a resident of North Carolina. He alleges that Peter Slomianyj and North Carolina Subway Group, development agents of DAI and residents of North Carolina, are indispensable parties. Defendant in 3:94cv1108 *Doctor's Associates v. Giannini* is a resident of Pennsylvania. He alleges that J.B. Jung and Subway Development Corporation of Philadelphia, development agents of DAI and residents of Pennsylvania are indispensable parties. Defendants in *Doctor's Associates v. McCrary*, *Doctor's Associates v. Gillon*, *Doctor's Associates v. Smith*, *Doctor's Associates v. Riise*, and *Doctor's Associates v. Benton* are residents of Alabama. They allege that Bernardo Frausto and Subway Development of Northern Alabama, development agents for DAI and residents of Alabama are indispensable parties.

agreement." *Moses H.Cone Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 20 (1983). *See also Steinberg & Lyman v. Takacs*, 774 F. Supp. 885 (S.D.N.Y. 1991) (parties to an arbitration agreement must arbitrate even though there are other defendants to the action). There would be no prejudice to the various development agents by not joining them, as they are not parties to the agreement in question and the underlying litigation would proceed as to those parties even if the litigation as to Doctor's Associates and the defendants in this action was stayed. This action to enforce an agreement by the defendants to arbitrate does not require joinder of the additional parties.

The motions to dismiss in 3:94cv00349 *Doctor's Associates v. Distajo* (doc. #s 31, 33, 35, 37, 39 and 46) are denied in their entirety, as they relate solely to this issue of subject matter jurisdiction.

C) *Personal Jurisdiction/Venue*

Defendants contend that this court lacks personal jurisdiction over them and that venue is not proper.[2] These arguments are without merit. In accordance with the arbitration agreement, defendants "subjected [themselves] in advance, to the jurisdiction of the court within whose territorial jurisdiction the arbitration proceedings are to be had . . . ." *Hatzlachh Supply Inc. v. Moishe's Electronics, Inc.*, 828 F. Supp. 178, 185 (S.D.N.Y. 1993) (vacated on other grounds, *Hatzlachh*

---

[2] Defendants assert this argument in the following cases:

3:94cv00515 *Doctor's Associates v. Youmaran*

3:94cv00998 *Doctor's Associates v. Kane*

3:94cv00514 *Doctor's Associates v. Guerro*

3:94cv00803 *Doctor's Associates v. Brenes*

3:94cv01108 *Doctor's Associates v. Gianni*

3:94cv00516 *Doctor's Associates v. Shino*

3:94cv00517 *Doctor's Associates v. Loenneke*

3:94cv00349 *Doctor's Associates v. Distajo*

3:94cv00803 *Doctor's Associates v. Johnson*

*Supply, Inc. v. Moishe's Electronics, Inc.*, 848 F. Supp. 25 (S.D.N.Y. 1994)); *Farr & Co. v. Cia. Intercontinental De Navegacion De Cuba*, 243 F.2d 342, 346 (2d Cir. 1957). The arbitration agreement also includes a choice-of-forum clause, stating that the parties are to settle any disputes in Connecticut. Such advance consent waives any objection to personal jurisdiction and venue.

D) *Abstention*

Defendants contend, in a conclusory manner, that this court should decline to exercise jurisdiction over the matter under the doctrine of abstention, citing *Colorado River Water Conservation District v. United States*, 424 U.S. 800, 813-17 (1976).[3] Federal courts generally do not dismiss proceedings merely because the same matter is being litigated in state court. Only exceptional circumstances will compel a federal court to relinquish jurisdiction due to parallel proceedings in state court. *Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 13-14 (1983). Defendants claim that proceedings in over nine cases in state courts constitute compelling circumstances. There is nothing remarkable about parallel state litigation. Although it is not entirely clear how extraordinary the circumstances must be in order for the court to decline to exercise its jurisdiction in this context, it is clear that parallel proceedings alone is not sufficient. *See Id.*; Erwin Chemreinsky, *Federal Jurisdiction* at 669 (4th ed. 1989) (listing cases in which courts abstained due to varying circumstances). Defendants have not enumerated exceptional

---

[3] The following defendants assert this argument:

3:94cv00515 *Doctor's Associates v. Youmaran* (doc. #4)
3:94cv00803 *Doctor's Associates v. Brenes* (doc. #4)
3:94cv00514 *Doctor's Associates v. Guerro* (doc. #4)
3:94cv00516 *Doctor's Associates v. Shino* (doc. #6)
3:94cv00517 *Doctor's Associates v. Loenneke* (doc. #5)
3:94cv00349 *Doctor's Associates v. Distajo* (doc. #18 )
3:94cv00998 *Doctor's Associates v. Kane* (doc. #3)
3:94cv01108 *Doctor's Associates v. Gianni* (doc. #4)

circumstances that warrant dismissal in deference to the state court litigation.

E) *Res Judicata and Collateral Estoppel*

Defendant in *Doctor's Associates v. Johnson* alleges that res judicata or collateral estoppel precludes jurisdiction here over the matter because the North Carolina trial court in which a complaint was filed declined to stay the lawsuit. These orders are on appeal, and therefore they do not constitute a final judgment on the merits. Therefore res judicata does not apply. *See Allen v. McCurry*, 449 U.S. 90, 94 (1980). Collateral estoppel applies only to issues decided finally in another forum. *Jim Beam Brands Co. v. Crawford, Ltd.*, 937 F.2d 729, 734 (2d Cir. 1991). Even if these orders were to be considered final, a denial of a motion to stay does not preclude a petition to compel arbitration pursuant to § 4 of the FAA. *See In re Pahlberg Petition*, 131 F.2d 968, 969 (2d Cir. 19 ).

Defendants in *Doctor's Associates v. McCrary* allege that an Alabama state court has determined the arbitration clause to be void and unenforceable and therefore these issues may not be relitigated in this forum. There is currently pending a motion to reconsider the judgment in the state court. Consequently, there is not a final judgment, as discussed above, and the doctrines of res judicata and collateral estoppel do not apply.

4) *Motion for Preliminary Injunction*

Plaintiffs move for a preliminary injunction to enjoin defendants from moving forward with their respective cases in state court. Defendants claim that this court cannot grant the relief requested under the provisions of 28 U.S.C. § 2283 (the "Anti-Injunction Act").

The Anti-Injunction Act was promulgated to balance the tensions between state and federal courts in a dual system, eliminating inevitable friction that may occur when both state and federal courts entertain proceedings. As the Supreme Court has noted, state proceedings "should normally be

allowed to continue unimpaired by intervention of the lower federal courts, with relief from error, if any, through the state appellate courts and ultimately this Court." *Atlantic Coast Line R. Co. v. Locomotive Engineers*, 398 U.S. 281, 287 (1970).

Injunctions can issue against state proceedings in certain limited situations, "namely, when expressly authorized by statute, necessary in aid of the court's jurisdiction, or necessary to protect or effectuate the court's judgment." *Chick Kam Choo v. Exxon Corp.*, 486 U.S. 140, 146 (1988). The exceptions are narrow and "'not [to] be enlarged by loose statutory construction.'" *Id.* (quoting *Atlantic* 398 U.S. at 146). As there is neither statutory authority for entry of an injunction nor a judgment which the court seeks to effectuate, the question is whether this court can enjoin the state court proceedings in aid of its jurisdiction.

In the present action, the state and federal court have concurrent jurisdiction and consequently neither court is "free to prevent either party from simultaneously pursuing claims in both courts." *Atlantic* 398 U.S. at 295.

> Each court is free to proceed in its own way and in its own time, without reference to the proceedings in the other court. Whenever a judgment is rendered in one of the courts and pleaded in the other, the effect of that judgment is to be determined by application of the principles of res judicata.

*Vendo Co. v. Lektro-Vend Corp.*, 433 U.S. 623, 642 (1977). Additionally, the Supreme Court has limited the "in aid of jurisdiction" exception only to cases in which a federal court acquires jurisdiction over real property, but has not extended it to proceedings involving *in personam* jurisdiction. *Atlantic* 398 U.S. at 295-96. As the state court proceedings do not impair this court's jurisdiction to proceed, and there is no dispute as to real property, an injunction is not appropriate.

Exceptions to the Anti-Injunction Act recognized in the Second Circuit also do not apply to the present situation. The

Act has been found not to apply when state court proceedings have not been instituted. *Standard Microsystems v. Texas Instruments*, 916 F.2d 58, 61 (2d Cir. 1990). However, each of the consolidated cases have pending litigation in a state court, and the act bars "an injunction to stay *proceedings* in a State Court." 28 U.S.C. § 2283 (emphasis added). The Second Circuit has cast doubt as to the validity of another exception formulated in the Seventh Circuit in *Barancik v. Investors Funding corp.*, 489 F.2d 933 (7th Cir. 1973), which allowed an injunction if the state court proceedings were instituted after a motion was filed to enjoin it, but before the court ruled on it. *See Standard Microsystems*, 916 F.2d at 61. The facts here do not support such an argument as the state court litigation was commenced prior to plaintiff's application for a preliminary injunction.

The motion for a preliminary injunction (doc. # 59) is denied as the action does not fall within any of the narrow exceptions to the Anti-Injunction Act. Accordingly, defendants' motions to file responsive pleadings in state court are granted.

*Conclusion*

The following motions to dismiss are denied:

3:94cv00349 *Doctor's Associates v. Distajo* (doc. #s 4, 18, 31, 33, 35, 37, 39, 46, 53, 84, 86, 89)
3:94cv00369 *Doctor's Associates v. Gillon* (doc. #7)
3:94cv00370 *Doctor's Associates v. Smith* (doc. #5)
3:94cv00511 *Doctor's Associates v. Brenes* (doc. #4)
3:94cv00514 *Doctor's Associates v. Guerro* (doc. #4)
3:94cv00515 *Doctor's Associates v. Youmaran* (doc. #4)
3:94cv00516 *Doctor's Associates v. Shino* (doc. #6)
3:94cv00517 *Doctor's Associates v. Loenneke* (doc. #5)
3:94cv00803 *Doctor's Associates v. Johnson* (doc. #3)
3:94cv00948 *Doctor's Associates v. Kane* (doc. #3)
3:94cv01108 *Doctor's Associates v. Gianni* (doc. #4)
3:94cv01457 *Doctor's Associates v. Papaleo* (doc. #5)

The following motions for a hearing are denied:

3:94cv00349 *Doctor's Associates v. Distajo* (doc. # 21 & 50)

3:94cv00354 *Doctor's Associates v. McCrary* (doc. # 9)

3:94cv00369 *Doctor's Associates v. Gillon* (doc. # 9)

3:94cv00370 *Doctor's Associates v. Smith* (doc. # 8)

3:94cv00371 *Doctor's Associates v. Riise* (doc. # 10)

3:94cv00372 *Doctor's Associates v. Benton* (doc. # 8)

3:94cv00511 *Doctor's Associates v. Brenes* (doc. #8)

3:94cv00514 *Doctor's Associates v. Guerrero* (doc. #8)

3:94cv00515 *Doctor's Associates v. Youmaran* (doc. #8)

3:94cv00516 *Doctor's Associates v. Shino* (doc. #7)

3:94cv00517 *Doctor's Associates v. Loenneke* (doc. #8)

The following motions to file documents in pending state proceedings are granted: *Doctor's Associates v. Distajo* 3:94cv00349 (doc. #s 72, 73, 74, 77, 78, 79, 80). The motion for leave to file a supplemental memorandum of law in support of the motion to dismiss for lack of venue 3:94cv00511 *Doctor's Associates v. Brenes* (doc. #7) is granted, and was considered. The motion to transfer venue, *Doctor's Associates v. Distajo* 3:94cv00349 (#8), is denied. The motion for a preliminary injunction *Doctor's Associates v. Distajo* 3:94cv00349 (#59) is denied.

Any responsive pleadings to the petitions to compel arbitration shall be filed on or before October 14, 1994. The petitions shall be decided on the record as of that date.

SO ORDERED.

Dated at New Haven, Connecticut, this 29th day of September, 1994.

/s/ Peter C. Dorsey

United States District Judge

## APPENDIX D

[Filed December 9, 1994]

UNITED STATES DISTRICT COURT

DISTRICT OF CONNECTICUT

DOCTOR'S ASSOCIATES, INC. :

-vs- : Civil No. 3:94CV349 (PCD)

EMILY DISTAJO, ET AL. :

## RULING ON PENDING MOTIONS

After entry of a temporary restraining order prohibiting defendants from pursuing various state court actions, a hearing to show cause why a preliminary injunction should not enter was held on November 29, 1994. Defendants[1] move to vacate

---

[1] The following defendants bring this motion:

3:94cv01457 *Doctor's Associates v. Papaleo*
3:94cv01456 *Doctor's Associates v. Rothmund*
3:94cv00349 *Doctor's Associates v. Distajo*
3:94cv00516 *Doctor's Associates v. Shino*
3:94cv00514 *Doctor's Associates v. Guerrero*
3:94cv00948 *Doctor's Associates v. Kane*
3:94cv01108 *Doctor's Associates v. Giannini*
3:94cv00803 *Doctor's Associates v. Johnson*
3:94cv00517 *Doctor's Associates v. Loenneke*
3:94cv00515 *Doctor's Associates v. Youmaran*
3:94cv00511 *Doctor's Associates v. Brenes*

The "Alabama defendants" did not join in the motion. They are:

3:94cv00372 *Doctor's Associates v. Benton*
3:94cv00354 *Doctor's Associates v. McCrary*
3:94cv00370 *Doctor's Associates v. Smith*
3:94cv00371 *Doctor's Associates v. Riise*
3:94cv00369 *Doctor's Associates v. Gillon*

the temporary restraining order and oppose plaintiff's motion for preliminary injunction.

*Background*

Doctor's Associates, Inc. (DAI) the national franchisor of "Subway" sandwich shops, is a Florida corporation. DAI entered into written franchise agreements with defendants, permitting them to operate Subway shops. The agreements contain an arbitration clause (paragraph 10c) which reads:

> Any controversy or claim arising out of or relating to this contract or the breach thereof shall be settled by Arbitration in accordance with the Commercial Arbitration Rules of the American Arbitration Association at a hearing to be held in Bridgeport, Connecticut and judgment upon an award rendered by the Arbitrator(s) may be entered in any court having jurisdiction thereof. The commencement of arbitration proceedings by an aggrieved party to settle disputes arising out or relating to this contract is a condition precedent to the commencement of legal action by either party. The cost of such a proceeding will be borne equally by the parties.

Defendants have sued plaintiff, affiliated individuals and entities in various state courts. Plaintiff demanded arbitration of defendants' claims by the American Arbitration Association in accordance with the arbitration clause. Defendants have refused to arbitrate. The matter has been ordered to arbitration. Plaintiff has moved to enjoin defendants from proceeding in state court with parallel litigation.

*Discussion*

A) *Res Judicata/Collateral Estoppel*

Defendants argue that res judicata and/or collateral estoppel bar this court from deciding the arbitration issue. Specifically, they contend that an October 24, 1994 judgment of an Illinois

state court[2] prevents relitigation of the issue, as Illinois law recognizes a trial court judgment as final for purposes of res judicata and collateral estoppel.

The full faith and credit statute, 28 U.S.C. § 1738 gives state court judgments the same preclusive effect as given by courts of the forum state. *Marrese v. American Academy of Orthopaedic Surgeons*, 470 U.S. 373, 380 (1985). Illinois law thus determines what preclusive effect is to be given to the October 24, 1994 decision.

Under Illinois law, preclusive effect is given to a final judgment on the merits. *Pelon v. Wall*, 262 Ill. App.3d 131, 135 (1994). "For res judicata purposes, a judgment is not final until the possibility of appellate review has been exhausted." *Id.* (citations omitted). Plaintiff has indicated that there is a motion for reconsideration pending in the Illinois case. As that motion is pending, and there is the possibility of appeals, the Illinois judgment does not preclude this court from either acting on the arbitration issue or ordering appropriate measures to effectuate its decisions.

B) *Stay of State Court Proceedings*

1) *Federal Arbitration Act*

Defendants first argue that this court cannot stay the underlying state actions pursuant to § 3 of the Federal Arbitration Act (FAA) as that section only allows a court to stay a case when it has a pending suit before it. As there is no suit currently before the court, it is inappropriate for the court to use this section to stay litigation.

2) *Anti-Injunction Act*

Federal courts are generally prohibited from staying state court proceedings by the Anti-Injunction Statute, 28 U.S.C.

---

[2] Defendants also cite certain Alabama decisions. Defendants effected by those decisions do not challenge a preliminary injunction. Those decisions will not be discussed here.

§ 2283. However, the statute provides that "[a] court of the United States may not grant an injunction to stay proceedings in a State court except . . . to protect or effectuate its judgments." *Id.* This exception is applicable where "a federal court has made [a] conclusive ruling[] and [its] effect may be undermined by threatened relitigation in state courts." *Standard MicroSystems v. Texas Instruments*, 916 F.2d 58, 60 (2d Cir. 1990).

It has been held here that any dispute as to DAI, in accordance with the agreement, must be addressed in arbitration. Continued litigation of these issues in parallel state proceedings will undermine, if not moot, this ruling. Further proceedings as to defendants' disputes with DAI, which have been determined not to belong in the courts, but in arbitration, may effect this court's judgment. *Necchi Sewing Machine Sales Corp. v. Carl*, 260 F. Supp. 665, 669 (S.D.N.Y. 1966); *see also McGuire, Cornwell & Blakey v. Grider*, 765 F. Supp 1048, 1052 (D. Colo. 1991); *Hunt v. Mobil Oil Corp.*, 557 F. Supp. 368, 372 (S.D.N.Y. 1983).

Defendants have clearly manifested their intent to proceed with state court litigation despite the order of arbitration of their disputes with DAI. This continued action would impair the integrity of the order of arbitration. An injunction is not inappropriate.

*Conclusion*

The motion for preliminary injunction (doc. #120) is granted; the motion to vacate the temporary restraining order (doc. #127) is denied. Defendants shall be enjoined from proceeding with all related state court litigation pending arbitration.

SO ORDERED.

Dated at New Haven, Connecticut, this 9th day of December, 1994.

/s/ Peter C. Dorsey

United States District Judge

## APPENDIX E

[Filed May 3, 1994]

| | | |
|---|---|---|
| STATE OF NORTH CAROLINA | ) | IN THE GENERAL COURT OF JUSTICE |
| COUNTY OF GASTON | ) | SUPERIOR COURT DIVISION |
| Michael Johnson, | ) | FILE NO. 93 CVS 1324 |
| Plaintiff, | ) | |
| vs | ) | ORDER |
| Doctor's Associates, Inc., et al | ) | |
| Defendants. | ) | |

FINDINGS OF FACT:

1. This action was commenced by the Plaintiff's filing a complaint seeking damages for misappropriation of funds;

2. The Plaintiff is a franchisee of several Subway Sandwich store franchises in North Carolina. Doctor's Associates is the franchisor;

3. The franchise agreement contains an arbitration clause which provides as follows:

> C. Any controversy or claim arising out of, or relating to this contract, or the breach thereof, shall be settled by arbitration in accordance with the commercial arbitration of the American Arbitration Association at a hearing to be held in Bridgeport, Connecticut, or whichever City in which the company is then headquartered, and judgment upon an award rendered by the arbitrators may be entered in any court having jurisdiction thereof. The commencement of arbitration proceedings by an aggrieved party to settle disputes arising out of, or relating to this contract is a condition precedent to the commencement of legal action by either party.

4. In his complaint, Plaintiff alleges that the arbitration clause is void for illegality, lack of mutuality and fraud;

5. The Defendant Doctor's Associates, Inc., has filed a Motion to Dismiss for failure to state a claim and, in the alternative, a Motion to Stay the Proceedings pending completion of arbitration proceeding;

6. The hearing on these motions was held before the undersigned Judge;

7. After the hearing, the Court entered an order denying the Motion to Dismiss for failure to state a claim and ordering the parties to file supplemental briefs and affidavits on the issue of whether the Plaintiff waived his right to litigate by participating in arbitration;

Based on the evidence presented at the hearing, and as set forth in the supplemental affidavits, and after having considered the arguments of counsel, the Court makes the following additional findings of fact:

1. Doctor's Associates filed a demand for arbitration with the American Arbitration Association (AAA) on or about the 26th day of January 1993;

2. Attorney David W. Smith, III, acting on behalf of the Plaintiff, filed an answer and counterclaim on February 10, 1993, and also submitted a five hundred dollar administrative fee to the AAA;

3. In his answer the Plaintiff denied the allegations in Doctor's Associates' statement for arbitration and in his counterclaim, sought an award of damages based on his contention that an employee of Doctor's Associates had misappropriated the Plaintiff's funds. Plaintiff did not challenge the validity of the arbitration clause or object to the jurisdiction of AAA to arbitrate the parties' claims;

4. On April 7, 1993, Plaintiff filed an objection to the jurisdiction and authority of the AAA to proceed with arbitration. The basis for the objection was that the arbitration

provision in the franchise agreement was void and unenforceable because of illegality, lack of mutuality and fraud;

5. On April 14, 1993, pursuant to Rule 8 of the Commercial Arbitration Rules of the AAA, Plaintiff filed a motion with the AAA to amend its counterclaim. The motion was filed "under protest" and specifically set forth the bases on which the Plaintiff contested the jurisdiction of the AAA to arbitrate the matters. On the same date, the Plaintiff filed with the AAA a motion to appoint additional arbitrators;

6. The AAA is currently holding the matter in abeyance pending the decision of this Court on whether the parties are required to arbitrate or may litigate the issues in dispute;

7. To this point, the AAA has appointed one arbitrator but it has not ruled on the Plaintiff's motions to appoint additional arbitrators or the Plaintiff's motion to file an amended counterclaim;

8. The parties have not exchanged exhibits or witness lists nor has any evidence been taken in the arbitration;

BASED ON THE FOREGOING FINDINGS OF FACT, THE COURT MAKES THE FOLLOWING CONCLUSION OF LAW:

1. This Court has jurisdiction over the parties and the subject matter of this order;

2. The Plaintiff's limited participation in the arbitration proceedings did not constitute a waiver of his right to challenge the enforceability of the arbitration clause;

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED that Doctor's Associates' motions to dismiss or to stay these proceedings on the grounds that Plaintiff has waived his right to litigate the issues that are the subject of this action by participation in arbitration are denied.

This the 3rd day of May, 1994.

/s/ John Mull Gardner

Superior Court Judge Presiding

[Filed May 18, 1994]

| | |
|---|---|
| NORTH CAROLINA<br>GASTON COUNTY<br>MICHAEL JOHNSON,<br>Plaintiff,<br>vs.<br>DOCTORS ASSOCIATES, INC., a Florida Corporation (f/k/a DOCTORS ASSOCIATES, INC., a Connecticut Corporation); FREDERICK DELUCA, an individual; PETER BUCK, an individual; FRANCHISE WORLD HEADQUARTERS, INC., a Connecticut Corporation; PETER SLOMIANYJ, an individual; NORTH CAROLINA SUBWAY GROUP, INC., a North Carolina Corporation; DOUGLAS BENTELLE, an individual; SHEILA HALLETT, an individual; SANTO RHODES, an individual; MICHAEL ARMELLINO, an individual; and NANCY TIMMONS, an individual;<br>Defendants. | IN THE GENERAL COURT OF JUSTICE<br>SUPERIOR COURT DIVISION<br>93-CvS-1324<br><br>**AMENDED ORDER** |

Pursuant to Rule 60(a) of the North Carolina Rules of Civil Procedure, the May 3, 1994 Order entered in the captioned matter is hereby amended as follows:

1. Paragraph 5 of the Findings of Fact (beginning on page 1 of the Order) is stricken and is replaced with the following:

> 5. The Defendants Doctors Associates, Inc., Frederick Deluca, Peter Buck, Franchise World Headquarters, Inc., Peter Slomianyj and North Carolina Subway Group, Inc., have filed Motions to Dismiss for failure to state a claim and, in the alternative, Motions to Stay the Proceedings pending completion of arbitration proceedings;

2. Paragraph 7 of the Findings of Fact (on page 2 of the Order) is stricken and is replaced with the following:

> 7. After the hearing, the Court ordered the parties to file supplemental briefs and affidavits on the issue of whether Plaintiff waived his right to litigate by participating in arbitration;

3. The final paragraph of the Order is stricken and is replaced with the following:

> IT IS THEREFORE ORDERED, ADJUDGED AND DECREED that the Motions brought by all moving Defendants -- Doctors Associates, Inc., Frederick Deluca, Peter Buck, Franchise World Headquarters, Inc., Peter Slomianyj and North Carolina Subway Group, Inc., -- to dismiss or to stay these proceedings on the grounds that Plaintiff has waived his right to litigate the issues that are the subject of this action by participation in the arbitration are denied.

4. The May 3, 1994 Order shall remain the same in all other respects.

This the 17th day of May, 1994.

/s/ John Mull Gardner

Superior Court Judge Presiding

## APPENDIX F

[Filed May 18, 1994]

| | |
|---|---|
| NORTH CAROLINA<br>GASTON COUNTY | IN THE GENERAL COURT OF JUSTICE |
| MICHAEL JOHNSON,<br>Plaintiff,<br>vs.<br>DOCTORS ASSOCIATES, INC., a Florida Corporation (f/k/a DOCTORS ASSOCIATES, INC., a Connecticut Corporation); FREDERICK DELUCA, an individual; PETER BUCK, an individual; FRANCHISE WORLD HEADQUARTERS, INC., a Connecticut Corporation; PETER SLOMIANYJ, an individual; NORTH CAROLINA SUBWAY GROUP, INC., a North Carolina Corporation; DOUGLAS BENTELLE, an individual; SHEILA HALLETT, an individual; SANTO RHODES, an individual; MICHAEL ARMELLINO, an individual; and NANCY TIMMONS, an individual;<br>Defendants. | SUPERIOR COURT DIVISION<br>FILE NO. 93-CVS-1324<br>**ORDER** |

THIS MATTER coming on to be heard and being heard before the undersigned Superior Court Judge presiding at the February 28, 1994, Gaston County Civil Term of Court upon

Motions to Dismiss for failure to state a claim under Rule 12(b)(6) of the North Carolina Rules of Civil Procedure; such Motions being brought by defendants Doctors Associates, Inc., Frederick Deluca, Peter Buck, Franchise World Headquarters, Inc., Peter Slomianyj, and North Carolina Subway Group, Inc., by their respective counsel; and it appearing to the Court after arguments by counsel for all parties involved that the Complaint does state a claim;

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED that the moving Defendants' Motions to Dismiss for failure to state a claim pursuant to Rule 12(b)(6) of the North Carolina Rules of Civil Procedure be and hereby are denied.

This the 17th day of May, 1994.

/s/ John Mull Gardner

Superior Court Judge Presiding

## APPENDIX G

[Filed November 14, 1995]

**UNITED STATES COURT OF APPEALS**
FOR THE SECOND CIRCUIT
UNITED STATES COURT HOUSE
40 FOLEY SQUARE
NEW YORK 10007

GEORGE LANGE III
CLERK

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse, Foley Square, in the City of New York, on the 9th day of November one thousand nine hundred and ninety-five.

---

Doctor's Associates

Plaintiff-Appellee,

v

Dkt No: 94-9207

Distajo, et al.

Defendants-Appellants.

---

A petition for rehearing containing a suggestion that the action be *reheard* in banc having been filed herein by the appellant Emily Distajo, et al.

Upon consideration by the panel that decided the appeal, it is Ordered that said petition for rehearing is **DENIED**.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges for the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

**FOR THE COURT**

GEORGE LANGE III, Clerk

By: /s/ Beth J. Meador,

Administrative Attorney

p o ccc

inbancdn_frm

# APPENDIX H

## ARBITRATION

9 § 1

§ 1. "Maritime transactions" and "commerce" defined; exceptions to operation of title

"Maritime transactions", as herein defined, means charter parties, bills of lading of water carriers, agreements relating to wharfage, supplies furnished vessels or repairs to vessels, collisions, or any other matters in foreign commerce which, if the subject of controversy, would be embraced within admiralty jurisdiction; "commerce", as herein defined, means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation, but nothing herein contained shall apply to contracts of employment of seamen, railroad employees, or any other class of workers engaged in foreign or interstate commerce.

July 30, 1947, c. 392, 61 Stat. 670.

§ 2. Validity, irrevocability, and enforcement of agreements to arbitrate

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

July 30, 1947, c. 392, 61 Stat. 670.

§ 3. Stay of proceedings where issue therein referable to arbitration

If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

July 30, 1947, c. 392, 61 Stat. 670.

§ 4. Failure to arbitrate under agreement; petition to United States court having jurisdiction for order to compel arbitration; notice and service thereof; hearing and determination

A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any United States district court which, save for such agreement, would have jurisdiction under Title 28, in a civil action or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. Service thereof shall be made in the manner provided by the Federal Rules of Civil Procedure. The court shall hear the parties, and upon being satisfied that the making of the agreement for arbitration or the failure to comply therewith is not in issue, the court shall make an order directing the parties to proceed to arbitration in accordance with the terms of the agreement. The hearing and proceedings, under such agreement, shall be within the district in which the petition for an order directing such arbitration is filed. If the making of the arbitration

agreement or the failure, neglect, or refusal to perform the same be in issue, the court shall proceed summarily to the trial thereof. If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be in default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by the Federal Rules of Civil Procedure, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof.

July 30, 1947, c. 392, 61 Stat. 671; Sept. 3, 1954, c. 1263, § 19, 68 Stat. 1233.

## APPENDIX I

SUPREME COURT NO._____

IN THE SUPREME COURT
OF THE STATE OF ILLINOIS

| | |
|---|---|
| EMILY DISTAJO, RENATO DISTAJO, CONSTATINO LAMANDO, MILO LAMANDO, JOSE ALBERTO BRENES, ALVARO GUERRERO, MARIA T. GUERRERO, WESAN S. YOUMARAN, LINDA YOUMARAN, JULIE SHINO, JOHNSON SHINO, ALBERT YONAN, LEYLAH YONAN, LOUIS LOENNEKE, MARY ANN BOOKOUT, RONALD ROTHMUND, PATRICIA ROTHMUND, JOHN S. PAPALEO and J.S.P., Inc.<br>Plaintiffs-Movants,<br>v.<br>DOCTOR'S ASSOCIATES, INC., et al.,<br>Defendant-Respondent,<br>*and*<br>SANDRA BICKEL AND RAYMOND BICKEL,<br>Plaintiffs-Movants,<br>v.<br>DOCTOR'S ASSOCIATES, INC., et al.,<br>Defendant-Respondent, | Arising out of the following cases in the Third Judicial Circuit, Madison County, Illinois:<br>Cause Nos. 93-L-1293, 93-L-1294, 93-L-1295, 93-L-1296, 93-L-1297, 94-L-155, 94-L-799, 94-L-765<br>(Consolidated for pre-trial motion purposes)<br>The Honorable P. J. O'Neill, Circuit Judge Presiding<br><br>Arising out of Cause No. 94-L-1428 pending in the Circuit Court for the Third Judicial Circuit, Madison County Illinois.<br>The Hon. Phillip J. Kardis, Circuit Judge Presiding |

*and*

DONALD A. STUART, MARTIN SCHWARZE and D.A. STUART ENTERPRISES, INC.,

Plaintiffs-Movants,

v.

DOCTOR'S ASSOCIATES, INC., et al.,

Defendant-Respondent.

Arising out of Cause No. 95-L-1050 pending in the Circuit Court for the Third Judicial Circuit, Madison County, Illinois.

The Honorable P. J. O'Neill, Circuit Judge Presiding

**MOTION OF PLAINTIFFS-MOVANTS FOR A SUPERVISORY ORDER PURSUANT TO ILLINOIS SUPREME COURT RULE 383**

Of Counsel:

David M. Duree
**REINERT & DUREE, P.C.**
812 North Collins
Laclede's Landing
St. Louis, Missouri 63102-2174
(314) 621-5743

David M. Duree IBE # 697087
# 8 Deer Run
O'Fallon, Illinois 62269
(618) 624-2837

ATTORNEYS FOR PLAINTIFFS-MOVANTS

SUPREME COURT NO._____

IN THE SUPREME COURT
OF THE STATE OF ILLINOIS

| | |
|---|---|
| EMILY DISTAJO, RENATO DISTAJO, CONSTATINO LAMANDO, MILO LAMANDO, JOSE ALBERTO BRENES, ALVARO GUERRERO, MARIA T. GUERRERO, WESAN S. YOUMARAN, LINDA YOUMARAN, JULIE SHINO, JOHNSON SHINO, ALBERT YONAN, LEYLAH YONAN, LOUIS LOENNEKE, MARY ANN BOOKOUT, RONALD ROTHMUND, PATRICIA ROTHMUND, JOHN S. PAPALEO and J.S.P., Inc.<br><br>Plaintiffs-Movants,<br><br>v.<br><br>DOCTOR'S ASSOCIATES, INC., et al.,<br><br>Defendant-Respondent,<br><br>*and*<br><br>SANDRA BICKEL AND RAYMOND BICKEL,<br><br>Plaintiffs-Movants,<br><br>v.<br><br>DOCTOR'S ASSOCIATES, INC., et al.,<br><br>Defendant-Respondent, | Arising out of the following cases in the Third Judicial Circuit, Madison County, Illinois:<br><br>Cause Nos. 93-L-1293, 93-L-1294, 93-L-1295, 93-L-1296, 93-L-1297, 94-L-155, 94-L-799, 94-L-765<br><br>(Consolidated for pre-trial motion purposes)<br><br>The Honorable P. J. O'Neill, Circuit Judge Presiding<br><br>Arising out of Cause No. 94-L-1428 pending in the Circuit Court for the Third Judicial Circuit, Madison County Illinois.<br><br>The Hon. Phillip J. Kardis, Circuit Judge Presiding |

| | |
|---|---|
| *and* | ) |
| DONALD A. STUART, MARTIN SCHWARZE and D.A. STUART ENTERPRISES, INC., | ) Arising out of Cause No. 95-L-1050 pending in the Circuit Court for the Third Judicial Circuit, Madison County, Illinois. |
| Plaintiffs-Movants, | ) |
| v. | ) |
| DOCTOR'S ASSOCIATES, INC., et al., | ) The Honorable P. J. O'Neill, Circuit Judge Presiding |
| Defendant-Respondent. | ) |

## MOTION OF PLAINTIFFS-MOVANTS FOR A SUPERVISORY ORDER PURSUANT TO ILLINOIS SUPREME COURT RULE 383 AND SUGGESTIONS OF LAW IN SUPPORT

Come now Plaintiffs-Movants, and move the Court for entry of a supervisory order prohibiting Doctor's Associates, Inc. from relitigating the issues of the validity and enforceability of the arbitration clauses in the respective franchise agreements, under the doctrines of res judicata and preclusion, under Illinois law, until and unless the Illinois trial court judgments in favor of Plaintiffs on this issues are reversed or set aside pursuant to post-judgment motions and/or any appeals, on the following grounds:

### MOTION

1. Each of the ten groups of Plaintiffs entered into franchise agreements with Doctor's Associates, Inc., the national franchisor for Subway Sandwich Shops.

2. Each franchise agreement contains an arbitration clause requiring arbitration of all disputes in Connecticut.

3. Each Plaintiff operates, or previously operated, a Subway franchise shop within the state of Illinois.

4. Each Plaintiff filed a complaint in Madison County, Illinois, against Doctor's Associates, Inc., its development agents, leasing companies and owners, alleging fraud, breach

of contract, violation of the Illinois Franchise Disclosure Act and related claims.

5. In each case, after the Plaintiffs filed their respective Illinois state court lawsuits, Doctor's Associates, Inc. filed a complaint in the United States District Court of Connecticut, against each Plaintiff in Illinois, to compel the Illinois Plaintiffs-Connecticut Defendants-franchisees to arbitrate their claims against Doctor's Associates, Inc. in Connecticut pursuant to Section 4 of the Federal Arbitration Act, 9 U.S.C. § 4.

6. The Federal Arbitration Act does not confer independent federal jurisdiction.

7. The State and Federal courts have concurrent jurisdiction of actions under the Federal Arbitration Act.

8. Under current law, State court and Federal court actions between the same parties concerning the same issues may proceed simultaneously until one enters a binding judgment, which is then binding on the same parties in the other, parallel, case.

9. In the first eight Madison County, Illinois cases, the Circuit Court entered summary judgment in favor of the Plaintiffs, pursuant to Illinois Supreme Court Rule 304(a), on October 24, 1994. That summary judgment declared the respective arbitration clauses to be void and unenforceable for several alternative reasons including waiver, lack of mutuality and unconscionability.

10. A copy of that Illinois judgment is included in the Appendix as Exhibit A.

11. Doctor's Associates, Inc. filed a motion for reconsideration of the Madison County judgment of October 24, 1994. The motion for reconsideration was scheduled for hearing on November 23, 1994. On November 22, 1994, Doctor's Associates, Inc. filed a motion for a temporary restraining order and a petition for a preliminary injunction in the United States District Court of Connecticut, and the Connecticut District

Court entered the requested temporary restraining order. As a result Doctor's Associates, Inc.'s motion for reconsideration scheduled for hearing in Madison County, Illinois on November 23, 1994 was not heard, and remains pending. On December 9, 1994 the Connecticut District Court issued the preliminary injunction requested by Doctor's Associates, Inc. which remained in effect until the September 12, 1995 opinion of the Second Circuit Court of Appeals.

12. The first eight groups of Illinois Plaintiffs then argued in the Connecticut District Court that the prior Illinois state court judgment in their favor was entitled to full faith and credit under 28 U.S.C. § 1738 because, under the law of Illinois, Doctor's Associates, Inc. would be precluded from relitigating the issues of the enforceability and validity of the arbitration clauses until and unless the Illinois state court judgment was reversed or set aside by post-judgment motion and/or appeal.

13. On November 10, 1994 the Connecticut District Court entered orders compelling the first eight Illinois Plaintiffs to arbitrate their claims against Doctor's Associates, Inc. in Connecticut.

14. On December 9, 1994, the Connecticut District Court entered the above described preliminary injunction, enjoining the first eight groups of Plaintiffs/franchisees from continuing to litigate their Illinois lawsuits against Doctor's Associates, Inc., et al.

15. The ninth group of Plaintiffs/franchisees, the Bickels, filed a complaint against Doctor's Associates, Inc., et al., in Madison County, Illinois during December, 1994.

16. Doctor's Associates, Inc. immediately filed a lawsuit in the District Court of Connecticut to compel the Bickels to arbitrate their claims against it in Connecticut, pursuant to the Federal Arbitration Act, and immediately sought a preliminary injunction enjoining the Bickels from prosecuting their Illinois state court lawsuit.

17. Doctor's Associates, Inc. and its Illinois development agent, Subway Development of Chicagoland, Inc., each failed to enter their appearance, timely, in the Madison County, Illinois lawsuit.

18. On February 7, 1995, the Circuit Court of Madison County, Illinois entered a default judgment against Doctor's Associates, Inc. and Subway Development of Chicagoland, Inc. on the issue of liability, and scheduled a damage hearing for April 4, 1995. The court also entered a default judgment against Doctor's Associates, Inc. and Subway Development of Chicagoland, Inc. on Count IV of the Complaint for a Declaratory Judgment that the arbitration clause was void and unenforceable, and declared the arbitration clause to be void and unenforceable because it lacked mutuality, was unconscionable and did not meet the reasonable expectations of the parties under Restatement of Contracts, Second § 211. That default judgment, with respect to the issue of enforceability of the arbitration clause, was issued pursuant to Illinois Supreme Court Rule 304(a).

19. A copy of that judgment is included in the Appendix as Exhibit B.

20. The Bickels filed a copy of that judgment with the Connecticut District Court, arguing that it was entitled to full faith and credit under 28 U.S.C. § 1738.

21. Six days later, on February 13, 1995, the Connecticut District Court entered orders compelling the Bickels to arbitrate their claims against Doctor's Associates, Inc. in Connecticut and enjoining them from further prosecution of their Madison County, Illinois lawsuit. The injunction contained an exception that Doctor' Associates, Inc. could move the Madison County, Illinois Circuit Court to set aside the default judgment.

22. After February 13, 1995, Doctor's Associates, Inc. filed a motion to set aside the February 7, 1995 default judgment against it, in Madison County, Illinois. That motion was briefed by both sides, and each side presented oral argument

on April 4, 1995. That motion is currently under submission to the Madison County Circuit Court.

23. During the spring of 1995, Donald Stuart, Martin Schwarze and D.A. Stuart Enterprises, Inc. filed a complaint against Doctor's Associates, Inc., et al. in Madison County, Illinois, alleging fraud, violation of the Illinois Consumer Protection Act, breach of contract and violation of the Illinois Franchise Disclosure Act, among other claims, and also alleging that the arbitration clauses in the franchise agreements were unenforceable for several, alternative, reasons.

24. Thereafter Doctor's Associates, Inc. filed a complaint in the United States District Court for Connecticut to compel Donald Stuart, et al. to arbitrate their claims against Doctor's Associates, Inc. in Connecticut pursuant to the Federal Arbitration Act.

25. On July 21, 1995 the Madison County Circuit Court entered a judgment pursuant to the motion for summary judgment of Donald A. Stuart, et al. on their count for a declaratory judgment that the arbitration clause was void and unenforceable, declaring the arbitration clauses to be void and unenforceable for several, alternative, reasons, including lack of mutuality, unconscionability and failure to meet the reasonable expectations of the parties under Restatement of Contracts, Second § 211. That judgment was also entered under Illinois Supreme Court Rule 304(a).

26. A copy of that Madison County judgment is included in the Appendix as Exhibit C.

27. On July 27, 1995, and thereafter, the United States District Court for Connecticut entered a series of orders, rulings and judgments, ordering Donald Stuart and Martin Schwarze to arbitrate their complaints against Doctor's Associates, Inc. in Connecticut and enjoining them from further prosecution of their Madison County, Illinois lawsuit.

28. All ten groups of Illinois Plaintiffs/franchisees appealed the orders and judgment of the Connecticut District

Court to the United States Court of Appeals for Second Circuit.

29. The appeals of the first eight groups of Illinois Plaintiffs (Distajo, et al.) and the Bickels (two appeals) were heard in tandem by the Second Circuit Court of Appeals which issued its opinion on September 12, 1995. The Distajo appeal also included the appeals of five Subway franchisees from Alabama, one Subway franchisee from North Carolina, one Subway franchisee from Massachusetts and one Subway franchisee from Pennsylvania.

30. A copy of that opinion is set forth in the Appendix as Exhibit D.

31. The Second Circuit Court of Appeals reversed the Connecticut District Court on all nine orders compelling the first nine groups of Illinois franchisees (Distajo, et al. and Bickel) to arbitrate their disputes in Connecticut and also reversed all nine injunctions enjoining the first nine groups of Illinois Plaintiffs from prosecuting their Illinois State Court lawsuits and remanded those cases to the Connecticut District Court for further findings of fact on the fraud, waiver and alter-ego issues with respect to the enforceability and/or validity of the arbitration clauses.

32. On the full faith and credit issue, the Second Circuit ordered the Connecticut District Court to dismiss the Petition to Compel Arbitration against one on the five groups of Alabama franchisees, John McCrary (see Exhibit D at pages 14-20).

33. The Second Circuit, however, ruled that the prior Illinois state court judgments were not entitled to full faith and credit under 28 U.S.C. § 1738. See Exhibit D at pages 20-22.

34. The Second Circuit Court of Appeals was required to interpret and apply Illinois law to determine whether, under the law of Illinois, the prior Illinois judgments entered under Illinois Supreme Court Rule 304(a) would have preclusive effect, barring Doctor's Associates, Inc. from relitigating the

issues of the enforceability and/or validity of the arbitration clauses.

35. The Second Circuit Court of Appeals concluded that Illinois law would not bar Doctor's Associates, Inc. from relitigating the issues of the enforceability of the arbitration clauses until after all appeals, in Illinois, were exhausted.

36. Plaintiffs-movants submit that the Illinois common law and an Illinois Statute each would preclude Doctor's Associates, Inc. from relitigating the issues of the enforceability and validity of the arbitration clauses until and unless the Illinois trial court judgments, entered under Illinois Supreme Court Rule 304(a), are reversed or set aside pursuant to post-judgment motion and/or appeal, and that the Second Circuit Court of Appeals simply overlooked or misinterpreted Illinois law.

37. 28 U.S.C. § 1738 requires the Connecticut District Court, and the Second Circuit Court of Appeals, to give full faith and credit to the Illinois state court judgments at issue here if, under the law of Illinois, those judgments would have preclusive effect, preventing Doctor's Associates, Inc. from relitigating the issues decided in Illinois, until and unless those judgments are reversed by post-judgment motion and/or appeal.

38. On the other hand, if those Illinois trial court judgments would not have preclusive effect under the law of Illinois, the Connecticut District Court and the Second Circuit Court of Appeals are not required to give full faith and credit to the Illinois trial court judgments.

39. Donald Stuart and Martin Schwarze have also appealed the decisions of the Connecticut District Court ordering them to arbitrate and enjoining them from prosecuting their Illinois lawsuit, to the Second Circuit Court of Appeals. That appeal is still pending. Briefs have not yet been filed and oral argument is not yet scheduled.

40. The first nine groups of Plaintiffs/franchisees (including the Bickels) have filed Petitions for Rehearing in

the Second Circuit Court of Appeals on the issues of their jury trial demands, their contention that the Connecticut District Court did not have subject matter jurisdiction under the Federal Arbitration Act and their contention that the prior Illinois trial court judgments would have preclusive effect in Illinois and therefore are entitled to full faith and credit.

41. A copy of the Petition for Rehearing in the Bickel appeal is included in the Appendix as Exhibit E.

42. An essentially identical Petition for Rehearing was filed in the Second Circuit Court of Appeals in the Distajo, et al. appeal.

43. Doctor's Associates, Inc. also appealed the Madison County judgment in the Donald Stuart case to the Illinois Court of Appeals for the Fifth District. Doctor's Associates, Inc. then moved for and obtained a stay of that appeal because of the Connecticut District Court injunction against Donald Stuart, et al.

44. This is not a request for an advisory opinion. If the Illinois Supreme Court grants this motion for a supervisory order and enters such order declaring that the Madison County, Illinois state court judgments do have preclusive effect in Illinois, those judgments must be given full faith and credit by the Connecticut District Court and the Second Circuit Court of Appeals.

45. If such order is entered by the Illinois Supreme Court prior to the appellate decision in the pending appeal of Donald Stuart, et al. to the Second Circuit Court of Appeals, the supervisory order will materially advance pending Illinois cases because it would permit the prior Illinois trial court decision in the Donald Stuart case to be reviewed by the Illinois Appellate and/or Supreme Court. Mr. Stuart's Subway franchise stores are located in Madison County, Illinois.

46. The requested Illinois Supreme Court supervisory order would also materially advance the pending Illinois cases involving the other nine groups of Illinois franchisees/Plaintiffs here in that, in the event the opinion of the

Second Circuit Court of Appeals stands as is, that case will be remanded to the Connecticut District Court for further proceedings. An order stating that the Illinois trial court judgments do have preclusive effect in Illinois would be binding upon the Connecticut District Court in any proceedings after remand and any subsequent additional appeals to the Second Circuit Court of Appeals.

47. A key issue in the Connecticut District Court and the Second Circuit Court of Appeals is whether, under Illinois law, the prior Illinois trial court judgments would have preclusive effect barring Doctor's Associates, Inc. from relitigating, with respect to the same Plaintiffs/franchisees, the issues of the enforceability and validity of the arbitration clauses.

48. Accordingly, an Illinois Supreme Court supervisory order declaring that those trial court judgments have preclusive effect under the law of Illinois would materially advance ten separate cases pending in the state trial courts of Illinois and one appeal pending in the Illinois State Court of Appeals for the Fifth District.

49. On the other hand, in the event this request for a supervisory order is denied on any grounds other than the Illinois trial court judgments do not have preclusive effect under Illinois law, the Plaintiffs, Illinois franchisees, will be denied the right to pursue their claims and cases in the courts of Illinois because of a misinterpretation of Illinois law by the Connecticut District Court and the Second Circuit Court of Appeals.

50. Five state court judgments have been entered finding the arbitration clauses of Doctor's Associates, Inc. void and unenforceable in twelve separate cases. One such judgment (one case) was entered in Alabama, one judgment (one case) was entered in North Carolina and three judgments (ten cases) were entered in Illinois. These decisions are consisted with prior Illinois appellate decisions on the enforceability of the arbitration clauses of Doctor's Associates, Inc. Current Illinois Supreme Court Justice Harrison wrote the opinion in *Yates v. Doctor's Associates, Inc.*, 193 Ill.App.3d 431, 549

N.E.2d 1010 (Ill. App. 1990), in which the court found that the leasing companies were nothing more than the alter-egos or agents of Doctor's Associates, Inc. and that therefore, eviction lawsuits filed by the leasing companies, to resolve issues under the franchise agreements, waived the rights of Doctor's Associates, Inc. to compel arbitration of issues raised in complaints filed by the franchisees. In another case the Illinois Court of Appeals affirmed a trial court judgment of $200,000.00 actual damages and $1,000,000.00 punitive damages in favor of the franchisee and against Doctor's Associates, Inc. in which the franchisee claimed that Doctor's Associates, Inc. fraudulently misrepresented its method of resolving disputes, among other claims. *Cox v. Doctor's Associates. Inc.*, 245 Ill.App.3d 186, 613 N.E.2d 1306 (Ill. App. 1993), Petition for leave to appeal denied, 152 Ill.2d 556 (1993), cert. denied, 114 S.Ct. 1069 (1994).

Wherefore, for these reasons, all ten groups of Plaintiffs/franchisees move the Illinois Supreme Court for a supervisory order that the prior Illinois trial court judgments entered under Illinois Supreme Court Rule 304(a) have preclusive effect, barring Doctor's Associates, Inc. from relitigating the issues of the enforceability and validity of the arbitration clauses until and unless those Illinois trial court judgments are reversed or set aside pursuant to post-judgment motions and/or appeals.

## SUGGESTIONS OF LAW

The Federal Arbitration Act, 9 U.S.C. § 1 et seq., does not provide for independent Federal Court subject matter jurisdiction. The State and Federal Courts have concurrent jurisdiction over actions filed under the Federal Arbitration Act. *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 25, 74 L.Ed.2d 765, 786, 103 S.Ct. 927, Footnote 32 (1983).

State and Federal Court actions, between the same parties, on the same issues, may proceed simultaneously until a judgment is entered in one, binding the other under the principles of res judicata, collateral estoppel and/or the full faith and

credit statute. 28 U.S.C. § 1738. *McClellan v. Carland*, 217 U.S. 268, 282, 30 S.Ct. 501, 504-505, 54 L.Ed. 762 (1910); *Stanton v. Embrey*, 93 U.S. 548, 554, 23 L.Ed. 983 (1877); *University of Maryland v. Peat, Marwick, Main & Co.*, 923 F.2d 265, 275, 276 [7] (3rd Cir. 1991), after remand, and a second appeal, affirmed in part and reversed in part, on other grounds, *University of Maryland v. Peat, Marwick, Main & Co.*, 996 F.2d 1534 (3rd Cir. 1993).

All Madison County judgments at issue here were entered pursuant to Illinois Supreme Court Rule 304(a), 134 Ill.2d R. 304(a), and Illinois Supreme Court Rule 272, 134 Ill.2d R. 272. These judgments were therefore final trial court judgments for purposes of appellate review and for purposes of res judicata. *Village of Niles v. Szczesny*, 13 Ill.2d 45, 48, 147 N.E. 2d 371 (Ill. 1958); *Relph v. Board of Education*, 84 Ill.2d 436, 420 N.E.2d 147, 149, 150 [4-7] (Ill. 1981); *In re Marriage of Verdung*, 126 Ill.2d 542, 535 N.E.2d 818, 823 [7] (Ill. 1989).

*Relph v. Board of Education*, 84 Ill.2d 436, 420 N.E.2d 147, 149 [1-3] (Ill. 1981) specifically held:

> "(at 420 N.E.2d 149)
>
> The judgment of a court of competent jurisdiction, although it may be erroneous, is binding upon the parties *until reversed* and cannot be collaterally attacked.
>
> **********
>
> However, before the judgment can stand as a bar to subsequent to actions, under the doctrine of *res judicata* the first action must result in a *final judgment* on the merits. (Emphasis added.) * * * A judgment is final if it determines the litigation of the merits so that *if affirmed* the only thing remaining is to proceed with the execution on the judgment. *Village of Niles v. Szczesny*, (1958), 13 Ill.2d 45, 48, 147 N.E.2d 371. (Emphasis added).
>
> (at 420 N.E.2d 150)

> The *judgments of the appellate court were not final judgments* in the sense that they *did not terminate the litigation* but remanded the cases to the trial courts with directions that judgments be entered, which judgments, in turn, would be appealable to the appellate court under our constitution. The appellate court's decisions, in turn, would be subject to review by this court through petitions for leave to appeal. (73 Ill. 2d R. 315(a).) Since the judgments in these cases were still subject to the appellate process, they were not to be given *res judicata* effect. The most that can be said of the appellate court's mandate in each case is that it established *the law of the case*." (Emphasis added).

Plaintiffs-movants respectfully submit that *Relph v. Board of Education* was not intended to overrule *Harding Co. v. Harding*, 352 Ill. 417, 426[4], 186 N.E. 152 (Ill. 1933) where the Illinois Supreme Court held:

> "The doctrine of res judicata is, that a cause of action finally determined between the parties on the merits, by a court of competent jurisdiction, cannot again by litigated by new proceedings before the same or any other tribunal, *except as the judgment or decree may be brought before a court of appellate jurisdiction* for review in the manner provided by law." (Emphasis added).

The Illinois Supreme Court continued at 352 Ill. 417, 426:

> "A judgment or decree so rendered is a complete bar to any subsequent action on the same claim or cause of action, between the same parties or those in privity with them. This doctrine extends not only to the questions actually decided but to all grounds of recovery or defense which might have been presented."

The Illinois Supreme Court then distinguished defensive collateral estoppel from res judicata, 352 Ill. 417, 427, as follows:

> "When the second action between the same parties is upon a different cause of action, claim or demand, it is well settled that the judgment in the first suit operates as an estoppel only as to the point or question actually litigated and determined and not as to other matters which might have been litigated and determined."

Plaintiffs-movants respectfully submit neither *Relph v. Board of Education*, 84 Ill.2d 436, 420 N.E.2d 147 (Ill. 1981) nor *Ballweg v. City of Springfield*, 114 Ill.2d 107, 499 N.E.2d 1373 (1986) were intended to overrule the principles set forth in *Harding Co. v. Harding*.

*Relph v. Board of Education* involved issues which were more "law of the case" issues than res judicata. Only one lawsuit was filed by each school teacher in that case. The issue was whether an intermediate Appellate Court opinion/judgment, reversing a summary judgment in favor of the Defendant school district, barred the trial court, after remand, from considering changes in the law resulting from a subsequent Illinois Supreme Court decision in another case and whether that intermediate Appellate Court opinion/judgment barred the Plaintiff, in one of the cases, after remand, from amending her complaint to add a claim for damages.

The issue in *Ballweg v. City of Springfield* is also different than the issue presented by this motion. In *Ballweg v. Springfield*, a pleasure sailing boat pilot was injured and two passengers killed when the mast came into contact with low-hanging power lines. Two lawsuits were brought against the boat manufacturer. *Ballweg v. Springfield* was an action brought on behalf of one of the decedents. *Ogg v. City of Springfield*, 121 Ill.App.3d 25, 458 N.E.2d 1331 (Ill. App. 1984) is the related action brought on behalf of the other decedent and the surviving boat pilot. In *Ogg v. Springfield*, the jury returned a verdict in favor of that decedent's estate for

$100,000.00 and in favor of the surviving boat pilot for $175,000.00 and denied the claims for punitive damages. The appeal from *Ogg v. Springfield* was pending when *Ballweg v. Springfield* went to trial. Both cases involved the same accident.

In *Ballweg v. Springfield* the Plaintiff claimed *offensive collateral estoppel* against the boat manufacturer on the issue of liability. The trial court refused to apply collateral estoppel *offensively* because the appeal in *Ogg v. Springfield* was still pending.

In *Ballweg v. Springfield* the jury then returned a verdict for Plaintiff, against the manufacturer, for $304,388.35 in actual damages and $1,021,833.00 in punitive damages. The manufacturer appealed. The intermediate Court of Appeals reversed and remanded for a new trial. The Illinois Supreme Court granted review.

In *Ballweg v. Springfield*, the Illinois Supreme Court reversed the intermediate Court of Appeals, partially, and reinstated the jury verdict for actual damages of $304,388.35 and affirmed the Court of Appeals decision, partially, by denying the claim for punitive damages.

The *final result* in both *Ogg v. Springfield* and *Ballweg v. Springfield was the same*. Each of the three Plaintiffs recovered actual damages from the boat manufacturer but were precluded from recovering punitive damages.

Because of the Illinois Supreme Court ruling on other issues, it was not necessary for it to consider Plaintiffs' claim that the trial court erred in failing to apply the principles of offensive collateral estoppel on the issue of liability. Nevertheless, the Illinois Supreme Court did so, citing *Relph v. Board of Education* for the proposition that the trial court, in *Ballweg*, did not err in refusing to apply the principles of offensive collateral estoppel on the issue of liability because the prior judgment against the manufacturer in *Ogg v. Springfield* was still on appeal.

The Supreme Court also acknowledged that collateral estoppel is an *equitable doctrine* based upon the principles of judicial economy citing *Morris v. Union Oil Company*, 96 Ill.App.3d 148, 421 N.E.2d 278 (Ill. App. 1981).

By denying the offensive use of collateral estoppel while an appeal from the first judgment against the same Defendant was pending, under the facts of *Ballweg v. City of Springfield*, the Supreme Court did no harm to the *principles of judicial economy* because it arrived at the same decision, on other grounds, that it would have reached if it had applied the principles of offensive collateral estoppel.

Plaintiffs-movants respectfully submit that neither *Relph v. Board of Education* nor *Ballweg v. Springfield* overruled or reversed the rule set forth in *Harding Co. v. Harding*.

As stated in *Relph v. Board of Education*, and quoted above, in Illinois, the judgment of a court of competent jurisdiction, although it may be erroneous, is *binding upon the parties* until reversed and cannot be collaterally attacked.

Plaintiffs-movants respectfully submit that the District Court of Connecticut and the Second Circuit Court of Appeals misinterpreted Illinois law in concluding that a final trial court judgment, in Illinois, does not bar the same parties from relitigating the same issue in another case until all appeals of that final judgment have been exhausted. See pages 21 and 22 of the Second Circuit September 12, 1995 opinion set forth in Exhibit D of the Appendix.

*Relph v. Board of Education* establishes that a final trial court judgment becomes final for purposes of res judicata and for appellate review at the same time. That principle was reaffirmed, three years after *Ballweg v. City of Springfield* was decided, by the Illinois Supreme Court in *In re Marriage of Verdung*, 126 Ill.2d 542, 535 N.E.2d 818 (Ill. 1989). Under Doctor's Associates, Inc.'s interpretation of Illinois law, adopted by the United States District Court for Connecticut and by the Second Circuit Court of Appeals, a trial court judgment, in Illinois, would not become final for purposes of

appellate review, or for purposes of res judicata, until all appellate review had been exhausted. In other words, a trial court decision could not be reviewed until all review had been exhausted. Plaintiffs-movants respectfully submit that this is not the law of Illinois.

Illinois courts have applied the principles of the Restatement (Second) of Judgments, generally. See *Agriserve, Inc. v. Belden*, 268 Ill.App.3d 828, 643 N.E.2d 1193, 1194, 1195 [1-3] (Ill. App. 1994) where the court applied the principles of sections 24 and 25 of the Restatement (Second) of Judgments.

The Restatement (Second) of Judgments, § 13, Comment f (1990) provides:

> "A judgment otherwise final for purposes of the law of res judicata is not deprived of such finality by the fact that time still permits commencement of proceedings in the trial court to set aside the judgment and grant a new trial or the like, nor does the fact that a party has made such a motion render the judgment nonfinal. This is the case even when a statute or rule of court provides that the judgment cannot be executed upon or otherwise enforced during the period allowed for making such a motion and the further period until the motion if made is decided. The judgment ceases to be final if it is in fact set aside by the trial court, as it would be upon the granting of a motion for a new trial."

Plaintiffs-movants respectfully submit that the law of Illinois on res judicata and preclusion is essentially the same as Restatement (Second) of Judgments, § 13, comment f (1990). See *Harding Co. v. Harding*, *Relph v. Board of Education* and *In re Marriage of Verdung* as well as Illinois Supreme Court Rules 304(a) and 272.

Irrespective of the status of Illinois law on the *equitable doctrine* of collateral estoppel and/or the offensive use of the equitable doctrine of collateral estoppel, Plaintiffs-movants respectfully submit that Illinois law on the principles of res

judicata and/or preclusion, precludes *the parties* from relitigating an issue decided in a final trial court judgment until and unless that judgment is reversed or set aside during post-judgment motion proceedings and/or appeal.

Under the common law of Illinois, Doctor's Associates, Inc. can not relitigate the issues of the enforceability and validity of the arbitration clauses until and unless the final trial court judgments set forth in Exhibits A, B and C of the Appendix are reversed or set aside by post-judgment motion proceedings and/or appeal.

If Plaintiffs-movants are correct in their interpretation of Illinois law, the United States District Court for Connecticut and the Second Circuit Court of Appeals were required to give full faith and credit to those Illinois judgments under 28 U.S.C. § 1738.

Plaintiffs-movants further submit that the Illinois trial court final judgments set forth in Exhibits A, B and C of the Appendix have preclusive effect under Illinois law, by statute, in that Doctor's Associates, Inc. could not file another lawsuit in Illinois to relitigate those issues. 735 ILCS § 5/2-619(a)(3) requires dismissal of any subsequent lawsuit filed by Doctor's Associates, Inc. in Illinois to relitigate the issues decided in the three final trial court judgments set forth in Exhibits A, B and C of the Appendix.

This motion is brought under Illinois Supreme Court Rule 383, 134 Ill.2d R. 383.

This motion does not seek an advisory opinion which is prohibited in Illinois.

*People ex. rel. partee v. Murphy*, 133 Ill.2d 402, 550 N.E.2d 998, 1002 [5] (Ill. 1990) described an advisory opinion as follows:

> "As stated earlier, when it is apparent that an opinion cannot affect the result as to the parties or controversy before it, a court should not resolve the

> question merely for the sake of setting a precedent to govern future actions." (Citations omitted).

Plaintiffs-movants respectfully submit that the order they are requesting here would require the Connecticut District Court and/or Second Circuit Court of Appeals and/or United States Supreme Court to give full faith and credit to the Illinois trial court final judgments set forth in Exhibits A, B and C to the Appendix, which would permit those final judgments to be reviewed by the Appellate and/or Supreme Courts of Illinois in the normal fashion. The requested order could well determine whether these ten groups of Illinois franchisees will be entitled to litigate their pending claims in the state courts of Illinois or be required to arbitrate, at considerable expense, in Connecticut.

All Plaintiffs-movants have filed claims, in their Madison County, Illinois complaints, for violation of the Illinois Franchise Disclosure Act, 815 ILCS § 705/1 et seq. The Illinois Franchise Disclosure Act was enacted, in part, to protect franchisees from the conduct of large, national, franchisors. 815 ILCS § 705/2.

In attempting to interpret the Illinois Franchise Disclosure Act, Judge Posner of the Seventh Circuit, in *My Pie International, Inc. v. Debould, Inc.*, 687 F.2d 919, 922 [3] (7th Cir. 1982) stated:

> "Although this statute has been on the books for more than eight years, there has been virtually no judicial interpretation of it, and we must guess how the Illinois courts would resolve several novel issues under the act."

Five years later, in *Proimos v. Fair Automotive Repair, Inc.*, 808 F.2d 1273, 1276 [3] (7th Cir. 1987), Judge Easterbrook stated:

> "As we said in *My Pie*, 687 F.2d at 922, decided eight years after the passage of the Act, almost no state cases discuss the statute. Another four years have passed without a significant new case in the

> courts of Illinois on the subject. Either franchisors in Illinois are uncommonly law abiding and franchisees uncommonly placid, or *something is diverting cases away from the courts of Illinois.*"

Plaintiffs-movants respectfully submit that there are few cases, in Illinois, decided under the Illinois Franchise Disclosure Act because franchisors, almost invariably, insert arbitration clauses in their standard franchise agreements, requiring arbitration of disputes under the Illinois Franchise Disclosure Act in some distant state before arbitrators prequalified and partially selected by the American Arbitration Association. The American Arbitration Association, in turn, receives its repeat business from the franchisors, not the franchisees.

The American Arbitration Association charges filing fees as high as $5,000.00 simply for the privilege of filing a claim or counterclaim. The larger the amount claimed, the higher the filing fee. This tends to discourage the economically disadvantaged from filing large claims. The American Arbitration Association also regularly assesses processing fees which must be paid by the parties. The parties to arbitration must also pay the hourly charges of the arbitrators (typically lawyers). Illinois franchisees who are required to arbitrate in Connecticut must also pay travel and lodging expenses for themselves, their witnesses and their attorneys. A typical Subway franchisee must frequently "win" the arbitration in order to "break even". The American Arbitration Association will not permit a decision to be issued until all fees to it and the arbitrators have been paid. Arbitration before the American Arbitration Association is an extremely expensive method of resolving disputes. As a group, Subway franchisees are not sophisticated business people. A relatively low investment is required to become a Subway franchisee. Most Subway franchisees could be described as economically disadvantaged. They are usually working people who have saved or borrowed the amount needed for the initial investment. They then work, typically, in their own franchise stores.

Other courts have expressed frustration with the practice of Doctor's Associates, Inc. in requiring the franchisees to arbitrate their claims against it, before the American Arbitration Association, in Connecticut. In *Casarotto v. Lombardi and Doctor's Associates, Inc.*, 886 P.2d 931 (Mon. 1994), Justice Trieweiler, after authoring the majority 4-3 opinion, wrote a concurring opinion setting forth his personal views of this practice. See *Casarotto v. Lombardi and Doctor's Associates, Inc.*, 886 P.2d 931 at 939-941 (Mon. 1994). A copy of the three *Casarotto v. Lombardi and Doctor's Associates, Inc.* opinions are set forth in Exhibit F of the Appendix. The original Montana Supreme Court opinion was entered on December 15, 1994. On June 12, 1995 the United States Supreme Court granted certiorari and simultaneously vacated the Montana Supreme Court opinion and remanded the case for further consideration in light of *Allied-Bruce Terminix Companies, Inc. v. Dobson*. See Exhibit F and page 17 of Exhibit D in the Appendix. On August 31, 1995, Justice Trieweiler delivered the opinion of the Montana Supreme Court reissuing its original opinion. A copy of the slip opinion is included in Exhibit F of the Appendix. Further review by the United States Supreme Court is quite possible.

Plaintiffs-movants have not raised the same challenges to the enforcement of the arbitration clauses that were presented in *Casarotto v. Lombardi and Doctor's Associates Inc.* The Montana Supreme Court held that Montana's arbitration statute was not pre-empted by the Federal Arbitration Act, relying upon *Volt Information Sciences v. Board of Trustees of Leland Stanford Junior University*, 489 U.S. 468 (1989). Plaintiffs-movants do not contend that the Illinois Arbitration Act is not pre-empted by the Federal Arbitration Act. The original trial court judgment held that its decision was the same under the Illinois Arbitration Act and the Federal Arbitration Act, and therefore did not need to determine which applied. See Exhibit A of the Appendix. All of the defenses to arbitration asserted by Plaintiffs-movants are equally viable under the Federal Arbitration Act and the Illinois Arbitration Act.

Plaintiffs-movants also do not seek to change the current law on arbitration here. Plaintiffs-movants merely seek an order stating that the Illinois trial court final judgments set forth in Exhibits A, B and C of the Appendix are entitled to preclusive effect under the law of Illinois.

For the foregoing reasons, Plaintiffs-movants, respectfully move the court to issue a supervisory order that the final trial court judgments set forth in Exhibits A, B and C of the Appendix are entitled to preclusive effect under the law of Illinois and that the principles of res judicata bar Doctor's Associates, Inc. from relitigating the validity and enforceability of these arbitration clauses until and unless the Illinois trial court judgments are set aside or reversed by post-judgment motion proceeding and/or appeal.

Of Counsel:

David M. Duree
**REINERT & DUREE, P.C.**
812 North Collins
Laclede's Landing
St. Louis, Missouri 63102-2174
(314) 621-5743

/s/ David M. Duree IBE # 697087
# 8 Deer Run
O'Fallon, Illinois 62269
(618) 624-2837

ATTORNEYS FOR PLAINTIFFS-MOVANTS

STATE OF MISSOURI )
) ss
COUNTY OF ST. LOUIS )

David M. Duree, being duly sworn upon his oath, deposes and states that the facts set forth in the above and foregoing motion for a supervisory order are true and correct and that the documents attached to the motion as Exhibits A, B, C, D, E and F of the Appendix are true and correct copies of such documents and that this affidavit is made pursuant to 735 ILCS § 5/1-109.

/s/ David M. Duree

Subscribed and sworn to before me this 29th day of September, 1995.

My Commission Expires:

/s/ Kelly O. Padgitt
Notary Public

[Seal]

## NOTICE OF FILING AND PROOF OF SERVICE

The undersigned hereby certifies that the original and one copy of the Supervisory Order will be filed with the Illinois Supreme Court on Monday, October 2, 1995, and that one copy of the Supervisory Order has been served upon each Justice for the Illinois Supreme Court at the addresses set forth below, and that one copy of the Supervisory Order has also been served upon Defendant-Respondent, Doctor's Associates, Inc., by placing the same in the United States mail, postage pre-paid, and addressed to each Justice of the Illinois Supreme Court as set forth below, and addressed to, Edward Wood Dunham, as the attorney for Doctor's Associates, Inc., at the address set forth below: this 29th day of September, 1995.

/s/ David M. Duree

The Honorable Michael A. Bilandic
Chief Justice of the Supreme Court of Illinois
160 N. LaSalle Street, 20th Floor
Chicago, Illinois 60601

The Honorable Benjamin K. Miller
Justice of the Supreme Court of Illinois
First of America Center, Suite #560
One North Old State Capitol Plaza
Springfield, Illinois 62701

The Honorable James D. Heiple
Justice of the Supreme Court of Illinois
110 N. Fifth Street, Suite #201
P.O. Box 997
Pekin, Illinois 61555

The Honorable Charles E. Freeman
Justice of the Supreme Court of Illinois
160 N. LaSalle Street, 20th Floor
Chicago, Illinois 60601

The Honorable Moses W. Harrison III
Justice of the Supreme Court of Illinois
333 Salem Place, Suite #170
Fairview Heights, Illinois 62208

The Honorable Mary Ann McMorrow
Justice of the Supreme Court of Illinois
160 N. LaSalle Street, 20th Floor
Chicago, Illinois 60601

The Honorable John L. Nickels
Justice of the Supreme Court of Illinois
1500 Lincoln Highway, Suite #201
St. Charles, Illinois 60174

Edward Wood Dunham
**WIGGIN & DANA**
One Century Tower
New Haven, Connecticut 06508-1832

ATTORNEY FOR DEFENDANT, RESPONDENT,
DOCTOR'S ASSOCIATES, INC.

## APPENDIX J

SUPREME COURT OF ILLINOIS
SUPREME COURT BUILDING
SPRINGFIELD 62701

JULEANN HORNYAK
CLERK OF THE COURT
(217) 782-2035
TELECOMMUNICATIONS
DEVICE FOR THE DEAF
(217) 524-8132

FIRST DISTRICT OFFICE
20TH FLOOR
160 NO. LASALLE ST.
CHICAGO 60601
(312) 793-1332
TELECOMMUNICATIONS
DEVICE FOR THE DEAF
(312) 793-1333

October 31, 1995

Mr. David M. Duree
Reinert & Duree, P.C.
812 North Collins
Laclede's Landing
St. Louis, Missouri 63102-2174

In re: Emily Distajo et al., movants, v. Doctor's Associates, Inc., et al, respondents. No. 79878.

Dear Mr. Duree:

The following order was entered on this date in the above captioned case:

The motion by movants for a supervisory order is *denied.*

Very truly yours,

/s/ Juleann Hornyak
Clerk of the Supreme Court

JH:jmb

cc: Mr. Edward Wood Dunham

## APPENDIX K

[United States District Court, District of Connecticut]

STATE OF MISSOURI )
) SS.
CITY OF ST. LOUIS )

## AFFIDAVIT

I, DAVID G. LOSEMAN, being duly sworn, state:

1. I am over the age of 18 years, understand the obligation of an oath, and have personal knowledge of the facts set forth in this affidavit. I am a member in good standing of the Missouri bar and Illinois bar, and admitted to practice before the United States District Court for the Central and Southern Districts of Illinois, the United States District for the Eastern District of Missouri, and the United States Court of Federal Claims.

2. I am an attorney with the law firm of Armstrong, Teasdale, Schlafly & Davis in St. Louis, Missouri which is acting as local counsel on behalf of Doctor's Associates, Inc. ("DAI"), and other defendants in a set of six lawsuits filed in Illinois state court by present and former Subway franchisees. Plaintiffs in those actions are represented by the St. Louis firm of Reinert, Duree & Crane.

3. On Friday, July 29, 1994, I was in the Circuit Court of Madison County, Illinois with Glenn Davis, a partner with Armstrong, Teasdale, Schlafly & Davis, for a hearing on defendants' Motion to Transfer the Illinois state court actions to Cook County, Illinois on forum non conveniens grounds. David M. Duree of Reinert, Duree & Crane appeared at the hearing on behalf of the plaintiffs.

4. Mr. Duree produced at the conclusion of the hearing a Motion for Partial Summary Judgment for a declaratory judgment, which he had filed that day, and which asserted that the arbitration clause in each of the Illinois plaintiffs' franchise agreements is unenforceable. After oral argument on the

motion to transfer, Mr. Duree requested that the Court set the Motion For Partial Summary Judgment for hearing as soon as possible within a week or two.

5. In response to Mr. Duree's request, Glenn E. Davis advised the Court that because he had never received or seen the Motion for Summary Judgment, and because Wiggin & Dana is acting as lead counsel in the matter, he would need to confer with co-counsel at Wiggin & Dana before discussing a hearing date. The judge presiding over the hearing, the Hon. P.J. O'Neill, indicated that he would, at an unspecified future date, set the matter for a hearing, but would permit defendants' attorneys adequate time to review and respond to the motion and speak with co-counsel.

6. In response to Judge O'Neill's comments, Mr. Duree stated, in words or substance, that his clients were in a "race to the courthouse" and that he needed to set his motion as quickly as possible in order to obtain a ruling before the Connecticut District Court could rule on DAI's petitions to compel arbitration. Mr. Duree also advised Judge O'Neill that the Motion for Partial Summary Judgment should be set quickly because the arbitrability question was not based on factual issues, but only questions of law.

FURTHER AFFIANT SAYETH NOT.

/s/ David G. Loseman

Subscribed and sworn to before me, a Notary Public, this 5th day of August, 1994.

/s/ Karen S. Newell
Notary Public

My Commission expires:

[Seal]